# WHITE PAPER
# ON
# FAIR MARKET VALUATION AND
# JUST COMPENSATION FOR RIGHTS-OF-WAY
# ACROSS TRIBAL LANDS

Presented by

FAIR ACCESS TO ENERGY COALITION

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## I. INTRODUCTION

The Fair Access to Energy Coalition ("FAIR") presents this White Paper addressing the question of what is fair and reasonable compensation for the acquisition and renewal of rights-of-way ("ROWs") across Indian lands held in trust for Indian tribes by the United States and other tribal lands subject to federal restrictions on alienation ("tribal lands").

This White Paper is prepared for submittal to the Secretaries of Energy and of the Interior to assist in the study required by Section 1813 of Public Law No. 109-58, the Energy Policy Act of 2005 ("Section 1813"). Section 1813 provides:

> SECTION 1813. INDIAN LAND RIGHTS-OF-WAY.
>
> (a) STUDY-
>
> (1) IN GENERAL- The Secretary [of Energy] and the Secretary of the Interior (referred to in this section as the "Secretaries") shall jointly conduct a study of issues regarding energy rights-of-way on tribal land (as defined in section 2601 of the Energy Policy Act of 1992 (as amended by section 503)) (referred to in this section as "tribal land").
>
> (2) CONSULTATION- In conducting the study under paragraph (1), the Secretaries shall consult with Indian tribes, the energy industry, appropriate governmental entities, and affected businesses and consumers.
>
> (b) REPORT- Not later than 1 year after the date of enactment of this Act, the Secretaries shall submit to Congress a report on the findings of the study, including--
>
> (1) an analysis of historic rates of compensation paid for energy rights-of-way on tribal land;
>
> (2) recommendations for appropriate standards and procedures for determining fair and appropriate compensation to Indian tribes for grants, expansions, and renewals of energy rights-of-way on tribal land;
>
> (3) an assessment of the tribal self-determination and sovereignty interests implicated by applications for the grant, expansion, or renewal of energy rights-of-way on tribal land; and
>
> (4) an analysis of relevant national energy transportation policies relating to grants, expansions, and renewals of energy rights-of-way on tribal land.

This White Paper addresses appropriate "standards and procedures for determining fair and appropriate compensation" as described in subsection (b)(2). FAIR will provide separate comments, data, and background information on other matters subject to the Congressionally mandated study.

## II. EXECUTIVE SUMMARY

### A. Section 1813 Responds to Indian Tribes' Increasingly Unreasonable Compensation Demands for Consents to Federal Rights-of-Way Grants.

Over time, Indian tribes and other Native American groups (collectively "tribes") have sought to use the leverage provided under the federal General Right-of-Way Act of 1948 and related right-of-way statutes to seek increasingly higher compensation for providing the tribal consent that is required by U.S. Department of the Interior regulations, 25 C.F.R. Part 169. As a result, many strategically-located tribes now demand compensation that both greatly exceeds fair market value-based amounts paid to private and federal and State government landowners and bears little or no relation to appraisals of the fair market value of the lands across which the rights-of-way pass. These out of control right-of-way practices will yield a massive cost "shock" that will be felt by America's already-burdened energy consumers. Further, exponentially increasing tribal right-of-way demands amount to hidden "taxation without representation." End users, including residential home and apartment owners, and commercial and industrial entities, have no recourse vis-à-vis tribal government because they have no representation and no voice in those forums. Undaunted by these deleterious impacts on distant consumers and the national economy, tribal advocates seek to support claims for extraordinary compensation by advancing valuation claims that are not based on legal authority or accepted appraisal principles.

These circumstances caused Congress to order a study of this issue, as provided in Section 1813 of the Energy Policy Act of 2005, Public Law No. 109-58. This White Paper serves to provide information to assist the Departments of Energy and of the Interior in the work Congress has mandated.

### B. Fair Market Value is the Uniform Federal Standard for Determining Value of Rights-of-Way.

Fair market value ("FMV") is the compensation standard generally applied to acquisitions of rights-of-way across private, federal and State-owned lands. FMV is recognized in the Bureau of Indian Affairs' regulations addressing appropriate valuation of rights-of-way. *See* 25 CFR § 169.12, *discussed in* Point V. When the United States acquires lands of U.S. citizens for federal projects, or when utilities acquire private lands for public uses under federal or State law, fair market value is the standard universally applied. *See* Point IV. Under federal law governing the valuation of rights-of-way granted to private entities on federal lands administered by the United States Bureau of Land Management ("BLM"), and National Forest lands administered by the United States Forest Service ("USFS"), fair market value principles have long been the benchmark for valuation of rights-of-way grants. *See* Point VI - VIII.

The courts have consistently rejected efforts to apply novel theories untethered to fair market value principles. FMV principles are fair to the right-of-way holder, provide a fair return to the landowner for use of the lands, and provide an ascertainable standard. FMV is the appropriate benchmark for valuing tribal rights-of-way.

In recent years, the dollars demanded, and frequently, though grudgingly, paid for tribal rights-of-way have diverged increasingly from FMV principles. Tribal leaders and representatives have recognized their bargaining power under the current, standard-less laws and have sought to use rights-of-way "consent" payments as sources of funding to balance tribal budgets. Many tribes have demanded compensation tens or hundreds of times fair market value for the grant or renewal of rights-of-way. The Department of the Interior's regulation goes beyond statutory language, and requires tribal consent for all new rights-of-way, as well as renewals, and expansions. Moreover, the Department has not required tribes to maintain their consent (with respect to new grants and expansions) on terms that are reasonably aligned with fair market value methodology. As a consequence, the free flow of interstate commerce, including natural gas, liquid hydrocarbon products, and electricity, is threatened because right-of-way holders are unable to obtain rights-of-way, or the renewal of rights-of-way, on reasonable terms.

The result is that tribes are in a position to distort market signals by demanding "monopoly rents," limited only by the cost to build around tribal lands.[1] This monopoly power distorts energy users' consumption decisions and increases energy costs to society.

Applicants for rights-of-way or renewals and Indian tribes should negotiate fair and reasonable compensation in good faith based on fair market value appraisals and principles. This is particularly important when tribal lands are strategically located in relation to energy producing areas and the end user. However, such fair negotiations are challenged because of the absence of a level playing field -- a standard for valuing rights-of-way and a process that provides certainty, objectivity, transparency and finality. Congress should adopt a standard based on FMV and a clear process to define FMV for rights-of-way grants. If Congress concludes tribes should receive a premium due to sovereignty or other considerations, that premium must still be rooted in an objective standard. FMV is that standard. Fundamentally, Congress should eliminate the unfair negotiating advantage tribes enjoy and provide for a reasonable, ascertainable standard.

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[1] *See* FAIR's Economic Analysis of Standards for ROW Fees on Tribal Trust Lands, Attached as Exhibit A to this White Paper.

## III. FAIR ACCESS TO ENERGY COALITION AND ITS MEMBERS: BACKGROUND

FAIR has been established to bring reason to this unworkable right-of-way negotiation process. FAIR's membership includes energy providers and transporters, industry professionals, consumer groups and consumers who support a productive study of this important issue under section 1813. FAIR's members believe the study can serve as an important step in assuring that secure and reliable supplies of natural gas, electricity and petroleum products are available at reasonable prices.

## IV. FAIR MARKET VALUE, AS THE RECOGNIZED FEDERAL STANDARD, SHOULD BE THE VALUE BENCHMARK FOR RIGHTS-OF-WAY ACROSS TRIBAL LANDS.

### A. Fair Market Value is the Federal Standard.

FMV is the nationally recognized standard for determining compensation for interests in land required for the public good. An unimpeachable source of guidance on this is the set of standards the United States Department of Justice uses when it acquires property of U. S. citizens for rights-of-way and other uses needed for federal projects: the Uniform Appraisal Standards for Federal Land Acquisitions, developed by an Interagency Task Force and approved by the Department of Justice in 2000 ("Federal Appraisal Standards").[2] Pertinent portions of the Federal Appraisal Standards are attached as Exhibit B to this paper.

The "Purpose" section of the Federal Appraisal Standards provides a helpful starting point for this discussion:

> These Standards have been prepared for use by appraisers to promote uniformity in the appraisal of real property among the various agencies acquiring property on behalf of the United States. *It should make no difference to the landowner, whose property is being acquired, which agency is acquiring land, or what method of acquisition it uses.*

Federal Appraisal Standards, Purpose (emphasis added). By the same token, it should make no difference to a tribe whether a right-of-way is acquired directly by an agency of the United States or by an entity, for example, operating pursuant to a Certificate of Public Convenience and Necessity issued by the Federal Energy Regulatory Commission. The principles embraced in the Federal Appraisal Standards should apply with equal force to tribal lands rights-of-way regardless who seeks to acquire the easement.

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[2] *See* http://www.usdoj.gov/enrd/land-ack/yb2001.pdf. As the Forward to the Federal Appraisal Standards states, this is the Fifth Edition of the Standards, which were first published in 1971.

The Federal Appraisal Standards apply with equal force not only to full property acquisitions, but also to easement or right-of-way acquisitions. "Federal acquisitions involve a wide variety of easement types ranging from the traditional to the exotic; they include, for example, road, pipeline, [and] electric transmission line."[3] The Standards persuasively support an FMV basis for tribal rights-of-way.

**B. FMV Does Not Consider the Value to the Acquiring Entity.**

As the Federal Appraisal Standards specifically state, the *"Supreme Court has cautioned" that the value to the governmental user who is acquiring the land cannot be considered in determining "fair market value."* According to the Court, the value to the utility or government:

> must in fairness be eliminated [in determining fair market value], as where the formula is attempted to be applied as between an owner who may not want to part with his land because of its special adaptability to his own use, and a taker who needs the land because of its peculiar fitness for the taker's purposes. *These elements must be disregarded by the fact-finding body in arriving at 'fair' market value.*[5]

The Federal Appraisal Standards also state specifically that "highest and best use cannot be predicated on a demand created solely by the project for which the property is acquired . . .".[6]

Significantly, the "project enhancement rule" forecloses considering the use for which a right-of-way is being acquired in determining the "highest and best use" of the property being valued:

> The Supreme Court has recognized the existence of a "principle which excludes enhancement of value resulting from the government's special or extraordinary demand for the property." . . . The focal point of the "special or extraordinary" standard is that values resulting from the urgency or uniqueness of the government's need for the property or from the uniqueness of the use to which the property will be put do not reflect what a willing buyer would pay to a willing seller . . . .[7]

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[3] Federal Appraisal Standards at. 63-65, Section B-20, "Easements."
[5] *United States v. Miller*, 317 U.S. 369, 375 (1943) (emphasis added). *See* Federal Appraisal Standards at 30-31.
[6] Federal Appraisal Standards at 35.
[7] *United States v. Weyerhauser Co.*, 538 F.2d 1363, 1366 (9th Cir. 1976); see *also United States v. Chandler-Dunbar Co.*, 229 U.S. 53, 80-81 (1913); *United States v. 320.0 Acres of Land*, 605 F.2d 762, 811 n. 107 (5th Cir. 1979), *cited,* Federal Appraisal Standards at 35.

Consequently, the market value should be determined by sales of lands comparable to those being acquired for energy rights of way, not by formulas based on the energy transportation use to which the acquiring company will put the lands, which seek to appropriate the economic value of energy transportation. Alternative valuation methods, such as "corridor theories" some tribes have advanced, violate these precepts. *See* Point IX.

### C. Determining Fair Market Value under the Federal Appraisal Standards.

In the Federal Appraisal Standards, the United States Department of Justice has outlined how fair market value should be determined:

> Market value is the amount in cash, or on terms reasonably equivalent to cash, for which in all probability the property would have sold on the effective date of the appraisal, after a reasonable exposure time on the open competitive market, *from a willing and reasonably knowledgeable seller to a willing and reasonably knowledgeable buyer, with neither acting under any compulsion to buy or sell*, giving due consideration to all available economic uses of the property at the time of the appraisal.[8]

This definition is "based on a compendium of Supreme Court decisions regarding the definition of fair market value for federal eminent domain purposes."[9]

Further, the Standards state: "Where only an easement is acquired, the full fee value of the land within the easement is not necessarily a proper measure of diminution in value since the rights remaining in the owners may be very substantial."[10]

The market value is best reflected by "comparable sales": "[a]rms length transactions in lands in the vicinity of and *comparable to the land under appraisement*, reasonably near the time of acquisition, *are the best evidence of market value . . . .*" (emphasis added). The Federal Appraisal Standards recognize that "market value" and fair market value are synonymous. Federal Appraisal Standards at 30.[11] FMV is the value that is no more than fair or, as the Indian Right of Way Act requires, that is "just." BIA's requirement that tribes consent to rights-of-

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[8] Federal Appraisal Standards at 30 (emphasis added).

[9] *Id.*

[10] *Id.* at 63, n. 295, *citing United States v. An Easement and Right-of-Way Over Two Strips of Land*, 284 F. Supp. 71, 73 (W.D. Ky. 1968).

[11] *See United States v. Miller*, 317 U.S. 369, 374 (1943): "The owner has been said to be entitled to the 'value,' the 'market value,' and the 'fair market value' of what is taken. The term 'fair' hardly adds anything to the phrase 'market value' which denotes what 'it fairly may be believed that a purchaser in fair market conditions would have given,' or, more concisely,' market value fairly determined."

way grants or renewals potentially gives tribes monopoly power and, particularly at geographic "pinch points," prevents a market-driven FMV price. *See* FAIR's Economic Analysis, Exhibit A, at 3-8.

## V. THE GENERAL INDIAN RIGHT-OF-WAY ACT AND BIA RIGHT-OF-WAY REGULATIONS DO NOT PROVIDE TRIBES CARTE BLANCHE TO DEMAND EXCESSIVE COMPENSATION AS A CONDITION OF CONSENT.

Rights-of-way across tribal lands are granted by the Secretary of the Interior—not the tribe—though the Secretary's regulations require the tribe's consent to any grant or renewal. *See* 25 U.S.C. §§ 311, 312, 319, 320, 321, and 323; 25 CFR § 169.3. Concerning compensation, the generally applicable 1948 Indian Right-of-Way Act, 25 U.S.C. § 325, requires payment of "such compensation as the Secretary of the Interior shall determine to be just." "Just" means "right or fair, equitable, impartial." *Webster's New World Dictionary at 734. (3rd ed. 1988).* That simple Congressional language requires fairness to all parties—not an oppressive imposition by one party on the other.

The applicable BIA regulations call for rights-of-way to be granted for not less than the "*fair market value* of the rights granted, plus severance damages, if any, to the remaining estate."[15] The emphasized term has a defined meaning in federal and relevant state law. For tribal acquisition of interests in allotted lands, Interior has recognized that FMV is the lodestar determining value. *See* Point VII. However, for tribal lands, BIA lays emphasis on the "not less than" language of its regulation, taking the position that there can be no limit to the compensation a tribe may require for its consent. Under this rationale, BIA ignores the statutory language requiring that compensation be in an amount "the Secretary . . . *shall determine to be just*" and disclaims any responsibility to determine FMV and grant rights-of-way for a FMV-based value.[16] That position has allowed tribes to exact inflated compensation that operates effectively as a burdensome expropriation of funds by a tribe. Given the critical importance of energy transportation to national, state, local – and tribal – communities and economies, federal legislation should clarify that tribal rights-of-way for energy should be available for compensation grounded in the fair market value of the real property rights acquired. Moreover, the legislation should provide for certainty and finality in valuing rights-of-way and arranging for payment.

## VI. DEPARTMENT OF THE INTERIOR POLICIES FOR VALUING FEDERAL LANDS SUPPORT USING FAIR MARKET VALUATION PRINCIPLES FOR TRIBAL LANDS.

[15] 25 C.F.R. § 169.12 (2005) (emphasis added).

[16] BIA's ROW regulations allow rights-of-way generally to be "without limitation as to term of years. . . ". *See* 25 CFR § 169.18. However, tribes increasingly refuse to consent to any ROW or renewal longer than 20 years, and many are negotiating for considerably shorter periods.

The Department of the Interior has repeatedly reaffirmed that FMV principles should determine right-of-way value.

### A. Secretarial Order No. 3251

Pursuant to Secretarial Order No. 3251 (November 12, 2003), all Department of the Interior appraisals are required to be prepared based on the FMV principles of the Federal Appraisal Standards. This Order forecloses Department of the Interior officials from appraising tribal rights-of-way based on any of the tribes' creative alternative methods of valuation. Unfortunately, this policy and the Order have not been applied to prevent imposition of unreasonable compensation demands on holders of rights-of-way across tribal lands. A copy of Secretarial Order No. 3251 is attached as Exhibit C to this White Paper.

### B. Secretarial Order No. 3258

In Secretarial Order No. 3258, issued December 30, 2004, Secretary Norton provided "policy [guidance] for land valuation issues, real property appraisals, and legislative land exchanges." Section 4a(1) of the Order provides: "All real property appraisals performed by the Department shall conform to nationally recognized appraisal standards (*i.e.*, the Uniform Appraisal Standards for Federal Land Acquisitions and the Uniform Standards of Professional Appraisal Practice, as applicable). Accordingly, the use of public interest value, contingent valuation, habitat equivalency analysis and any other AMV [Alternative Methods of Valuation] in appraisals is expressly prohibited." A copy of Secretarial Order No. 3258 is attached as Exhibit D to this White Paper. Alternative Methods of Valuation are discussed in the next section.

### C. 2004 Department of Interior Policy on Alternative Methods of Valuation

As part of Secretarial Order No. 3258, Secretary Norton issued a "Policy on Alternative Methods of Valuation" ("AMV Policy"), which directly rejects valuation methods such as those tribes have recently advanced. In the AMV Policy, Secretary Norton observed:

> In recent years, some have asserted that non-market factors (*e.g.*, scenery, wildlife habitat, and conserved open space) also deserve consideration when transactions are negotiated. *Policy guidance is needed to clarify the distinction between market value appraisals and alternative methods of valuation (AMV) employed to assess non-market factors.*
>
> *In recent years, AMV have been advanced by those who assert that common measures of market value are unduly limiting. AMV are often*

*advocated by proponents of specific exchanges or acquisitions to support the application of a premium above a property's appraised value or, incorrectly, as a proxy for market value.*

The Secretary's Policy on AMV expressly rejects AMV methodology:

> All real property appraisals performed by the Department shall conform to nationally recognized appraisal standards (i.e., the Uniform Appraisal Standards for Federal Land Acquisitions and the Uniform Standards of Professional Appraisal Practice, as applicable). Accordingly, the use of public interest value, contingent valuation, habitat equivalency analysis, and *any other AMV in appraisals is expressly prohibited.*[18]

These statements should inform the Secretaries of the Interior and of Energy as they consider appropriate standards and procedures for determining value of federally granted rights-of-way across tribal lands. Tribal advocates seek to employ valuation methods, such as "corridor theories" of valuation, that impose a substantial premium over the property's value, or, under an "opportunity cost" rubric, they determine value by simply calculating the cost of building transportation or transmission facilities around the Indian reservation (a cost that bears no relation to the market value of the land, of course). Other tribes simply seek compensation that is orders of magnitude over a property's or right-of-way's market value. As FAIR's economic analysis reflects, current law puts a tribe in a monopolist's position as seller of needed ROW, and consumers and national energy policy suffer as a result. See FAIR's Economic Analysis, Exhibit A, attached. The Secretaries should not lose sight of the fact that these theories result in huge demands and huge payments that will be borne by America's energy consumers.

### D. 2005 Department of the Interior Office of Appraisal Services Memorandum

On May 31, 2005, the Department's Office of Appraisal Services issued a paper concluding that value for rights of way across Indian allotted lands should be determined by reference to the standards governing federal acquisitions of rights-of-way, based on a "before and after" methodology.[19] The Holley letter cited Section B-20 of the Federal Appraisal Standards. Significantly, Mr. Holley's letter cited the same regulation, 25 C.F.R. § 169.12, that addresses value for tribal rights-of-way. The Holley letter reflects the principle that right-of-way value must be determined under principles governing valuation of real property generally. Those principles include the application of market value standards, as described above.

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19 *See* May 31, 2005 Letter from Brian M. Holley, MAI, DOI National Business Center, Appraisal Services Directorate, Chief Appraiser, to OST/OAS [Office of Special Trustee, Office of Appraisal Services], Dept. of the Interior, attached as Exhibit D to this White Paper.

There is no sound reason these fair market valuation and appraisal principles should not apply to tribal lands. Tribal lands are used for economic activities, and the highest and best use of those lands is ascertainable. A tribe's economic loss when tribal lands are devoted to energy transportation is identical to that of non-tribal landowners. While tribes may have ties to lands based on traditional values and long associations, so may many non-tribal landowners, and neither federal nor state law makes special accommodations for such non-economic attachments. Moreover, tribes, like non-tribal landowners, are also beneficiaries of a flexible and functional energy transportation system, and it is fair for them to contribute rights-of-way needed for energy to flow smoothly and economically on terms comparable to those we require of others. At the very least, FMV principles should be a fundamental component in determining value of tribal lands for rights-of-way.

## VII. CONGRESS ESTABLISHED FMV AS THE STANDARD FOR TRIBAL ACQUISITION OF FRACTIONATED INDIVIDUAL INDIAN REAL PROPERTY INTERESTS, SUPPORTING APPLICATION OF FMV PRINCIPLES TO TRIBAL LANDS.

The Indian Land Consolidation Act ("ILCA")[20] provides, in pertinent part, that "[i]f the owner of an interest in trust or restricted land devises an interest in such land to a non-Indian under [the ILCA] the Indian tribe that exercises jurisdiction over the parcel of land involved may acquire such interest by paying to the Secretary the *fair market value* of such interest, as determined by the Secretary on the date of the decedent's death." (emphasis added).[21] Section 2214 of the ILCA, entitled "Establishing *fair market value*," then directs that:

> the Secretary may develop a system for establishing the *fair market value* of various types of lands and improvements. Such a system may include determinations of *fair market value* based on appropriate geographic units as determined by the Secretary. Such system may govern the amounts offered for the purchase of interests in trust or restricted lands under [§ 2205(c)(1)]. (emphasis added).

If fair market value is appropriate for Indian tribes and other Native American groups purchasing fractionated interests held by individual Indians, why should that principle not also apply to valuing rights-of-way across tribal lands?

In 1981 hearings before the Senate Select Committee on Indian Affairs, Kenneth L. Payton, Acting Assistant Secretary for Indian Affairs, and Senator Quentin Burdick of North Dakota had an exchange indicating that "fair market value" may be measured in the same fashion as "just compensation" in takings cases.[22]

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[20] 25 U.S.C. §§ 2201 - 2219.

[21] 25 U.S.C. § 2205(c)(1).

[22] Hearings on S. 503 Before the Select Committee on Indian Affairs, United States Senate, 97th Cong., 1st Sess., 20 (September 22, 1981)( (Senator Burdick: "Is the payment of fair

With the Indian Land Consolidation Act, Congress confirmed FMV as the appropriate standard for valuing Indian lands.

## VIII. FMV PRINCIPLES ARE CONSISTENTLY APPLIED TO VALUE RIGHTS-OF-WAY ON NON-INDIAN FEDERAL LANDS.

Right-of-way valuation methodology and rental obligations for rights-of-way on non-Indian Federal lands are founded squarely on principles of fair market value, without any sort of premium. This section of the White Paper discusses the provisions of federal law and regulation governing rights-of-way valuation on federal public lands administered by the BLM, on National Forest lands administered by the United States Forest Service, and on National Parks and other lands administered by the National Park Service. The Secretaries should give strong consideration to utilizing or drawing upon the valuation standards for rights-of-way across federal lands in determining the fair and appropriate compensation to be paid to Indian tribes for rights-of-way across tribal lands.

### A. Federal Policy Governing Rights-of-Way Valuation on Federal Lands Supports Application of FMV Principles to Tribal Lands.

The Congressional Declaration of Policy in the Federal Land Policy and Management Act ("FLPMA") states in part that "it is the policy of the United States that . . . the United States receive *fair market value* of the use of the public lands and their resources unless otherwise provided for by statute. . . ."[23] Generally, Subchapter V of FLPMA[24] addresses rights-of-way on federal public lands administered by the Bureau of Land Management ("BLM") and on National Forest lands administered by the U. S. Forest Service ("USFS"). Specifically, FLPMA Section 504[25] addresses the subject of right-of-way payments and valuation on BLM and USFS lands.

As amended in 1996, Section 504(g) provides in pertinent part: "The holder of a right-of-way shall pay in advance *the fair market value* thereof, as determined by the Secretary granting, issuing, or renewing such right-of-way. The Secretary concerned [either Interior for BLM lands or Agriculture for USFS lands] may require either annual payment or a payment covering more than one year at a time . . . ." Section 504(g) also authorizes the Secretaries to require the right-of-way applicant or holder to reimburse the United States for reasonable administrative and other costs incurred in processing an application and in the inspection and monitoring or construction, operation and termination of the right-of-way facilities.

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market value to those heirs adequate to meet any constitutional objection?" Mr. Payton: "I think so; yes.").

[23] 43 U.S.C. § 1701(a) (9) (emphasis added).

[24] 43 U.S.C. §§ 1761-1771.

[25] 43 U.S.C. § 1764(g).

Congress reiterated its policy applying FMV principles to rights-of-way on federal lands in the Energy Policy Act of 2005. Section 367 of the Energy Policy Act, titled "Fair Market Value Determinations for Linear Rights-of-Way Across Public Lands and National Forests," mandates that the Secretary of the Interior update valuation schedules to reflect current values - fair market values. According to a recent Advance Notice of Proposed Rulemaking that the BLM published, Section 367 "supplements existing Secretarial authority to assess and collect fair market value of the right to use, cross, or traverse public or [Forest Service] lands."[26]

### B. Bureau of Land Management Regulations and Policies for Public Domain Lands Also Apply FMV Principles for Rights-of-Way.

BLM's regulations governing rights-of-way across federal public domain lands, located at 43 C.F.R. Part 2800 (2004), also encompass and apply FMV principles. Under the new and old Part 2800 regulations, [27] BLM charges "rent" to holders of rights-of-way.[28] According to the Background discussion in the recent rule-making, the rental is:

> a charge for locating your right-of-way facility on public or Federal lands. It is payable (for a specified term) before we issue the grant and is based on the *fair market value* of the rights we authorize. We usually establish the rental for linear and communication sites on public lands via two separate administrative schedules. Based roughly on land values in the project area, these schedules are adjusted annually using an economic index.[29] (emphasis added).

For rental determination purposes, the BLM divides lands in the contiguous United States into eight zones.[30] For example, oil and gas or other energy pipeline rights-of-way on lands in McKinley and San Juan Counties, New Mexico -- counties in which the New Mexico portions of the Navajo Reservation are located -- are valued at $7.76 per acre per year (for Calendar Year 2005) and $8.01 per acre per year (for Calendar Year 2006).[31] This equates to $155.20 (2005 figure) or $160.20 (for 2006) for a 20 year period, without adjusting for inflation changes from year to year. It would appear that values in Northern Arizona counties, including counties in which the Navajo Reservation is located, are similar. There is no premium for large diameter pipelines and no discount for small diameter lines. The fees are fixed.

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[26] 71 Fed. Reg. 24836, at 24837 (April 27, 2006).

[27] The BLM amended the Part 2800 by final rule promulgated on April 22, 2005, that became effective June 21, 2005. 70 Fed. Reg. 20970 (April 22, 2005).

[28] *See, e.g.*, 43 C.F.R. § 2803.1-2 (2004); 43 C.F.R. § 2806.20 (April 22, 2005).

[29] 70 Fed. Reg. at 20971.

[30] *See* 43 C.F.R. §§ 2801.5 (definition of "zone") and 2806.20 (schedule of rents per acre by zone) (April 22, 2005). While BLM ROWs are often for terms of years, and not perpetual, its rental rates are to be based on FMV principles for the term involved. *See* 43 CFR § 2801.1-1(h) (ROW for a "reasonable term" ranging from one month to perpetual).

[31] These counties include lands within the Navajo Reservation in New Mexico.

The broad application of these principles is reinforced by the BLM Manual provisions addressing appraisals of real property. *See* BLM Manual Part 9310. Part 9310.01 describes the purpose of this part of the BLM Manual as establishing "real estate appraisal policy for estimating the market value of real property and estimating the market rent for use of public lands." The "objectives" of the Manual include establishing a "real property appraisal process [that] is designed to [p]rovide a credible and impartial procedure for estimating market value of real property, or interests therein."[32] According to the Manual, once an appraisal has been reviewed and approved in accordance with BLM policies, that "report may be used by the authorized officer for the following transactions . . . A. Rental payment for the use of Federally-owned real property . . . ."[33]

BLM Manual Section 9310.51.D. then instructs: "The appraiser and the approved estimate of market value *shall disregard any decrease or increase in the value of the real property prior to the date of valuation caused by the project for which such property is acquired,* or by the likelihood that the property would be acquired for such project, other than that due to physical deterioration within the reasonable control of the owner." (Emphasis added.). Efforts by tribes to use the existence of energy infrastructure built in an existing right-of-way to increase the value of lands subject to right-of-way negotiation or renegotiation are wholly inconsistent with the methods prescribed by these federal lands policies to value rights-of-way.

Further, in its recent Advance Notice of Proposed Rulemaking, the BLM expressed a policy preference that "right-of-way holders should be able to estimate rental payments and forecast changes in billed rent . . . ."[34] Allowing tribes to dramatically alter the economics of rights-of-way across tribal lands at the point of renewal is wholly inconsistent with Interior's policy.

### C. USFS Regulations and Policies for National Forest Lands Reserved from the Public Domain also apply FMV Principles.

The U.S. Forest Service's 36 C.F.R. Part 251 Subpart B regulations govern grants of rights-of-way and other special use permits on USFS lands. In USFS parlance, a right-of-way is generally referred to as an "easement" and is granted as a special use permit.[35] Under USFS regulations, annual rental fees are payable in advance.[36] Under some circumstances, fees for longer periods may be due.

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[32] BLM Manual Section 9310.02.A.
[33] BLM Manual at 9310.11.
[34] 71 Fed. Reg. at 24837.
[35] *See* 36 C.F.R. §§ 251.50, 251.51 (defining "easement" as including "linear rights-of-way" - which in turn is defined to include rights-of-way for roads, pipelines, transmission lines, fiber optic cables and the like.), and 251.53.
[36] *See* 36 C.F.R. § 251.57(a).

The annual rental fee "shall be based on the fair market value of the rights and privileges authorized, as determined by appraisal or other sound business management principles."[37] The term "sound business management principles" is defined as "accepted industry practices or methods of establishing fees and charges that are used or applied by the Forest Service to help establish the appropriate charge for a special use. Examples of such practices and methods include, but are not limited to, appraisals, fee schedules, competitive bidding, negotiation of fees, and application of other economic factors, such as cost efficiency, supply and demand, and administrative costs."[38] Rental fee payments also may be "adjusted whenever necessary: (1) As a result of fee review, reappraisal; or (2) upon a change in the holder's qualifications . . . ."[39]

The Forest Service's Manual regarding land appraisals describes the following "Objective": "The objective in appraising for land ownership adjustment, acquisition, and land use authorizations (land actions) is to *estimate values that are fair and equitable to the United States and the parties involved.* Usually the value sought is market value."[40] Forest Service policy is to "use market value, as defined in the [Federal Appraisal Standards], as the basis of any action that might result in the conveyance of title to any interest(s) in real property to or from the United States, unless another definition is required by law, regulation or policy."[41] As with the Forest Service's Manual, its Handbook acknowledges that "Market Value is the Standard."[42]

### D. National Park Service Regulations apply FMV Principles.

Even right-of-way regulations governing the grant of rights-of-way across National Park lands, compiled in 36 C.F.R. Part 14, provide for fair market valuation. For National Park lands rights-of-way, the regulation requires that "the charge for use and occupancy of lands under the regulations of this part will be the fair market value of the permit, right-of-way, or easement as determined by appraisal by the authorized officer."[43]

### E. The United States' Trust Responsibilities Do Not Require More than Fair Market Value

Fair market value concepts are not inconsistent with the federal trust responsibility regarding tribes and their lands. The federal trust doctrine requires the federal trustee to consider all factors relevant to its decisions, including the interests

[37] *See* 36 C.F.R. § 251.57(a)(1).
[38] *See* 36 C.F.R. § 251.51.
[39] *See* 36 C.F.R. § 251.57(g).
[40] Forest Service Manual, Chapter 5410.2 (emphasis added).
[41] *Id.*, Part 5410.3.5.
[42] *See* FSH 5409.12 - Appraisal Handbook, Chapter 10, Valuation Guidelines, Section 11.2 (February 15, 2005).
[43] 36 C.F.R. § 14.26.

of non-Indians and the impact of the decision on tribes' long term interests in economic development. The doctrine does not require the federal government to make all decisions in the manner that yields the most short-term cash to particular tribes. Several principles are instructive:

- Federal trust duties are defined by the applicable statute, not by abstract legal concepts. *See United States v. Navajo Nation*, 537 U.S. 488 (2003). The 1948 Indian Right of Way Act, 25 U.S.C. § 325, requires payment of "such compensation as the Secretary of the Interior *shall determine to be just*." (Emphasis added). That language implies fairness to, and reasonable conduct by, all parties.
- Federal courts applying the trust doctrine, even in the absence of specific language requiring balance such as that contained in the Indian Right-of-Way Act, require consideration of "all relevant factors." Those factors include the interests of parties that contract with tribes, and not whether prior agreements "were a good deal or a bad deal," for a tribe, nor to foster "a mere vehicle to achieve an ulterior objective otherwise unattainable."[44]
- The trust doctrine contemplates consideration of long-term economic development interests of all tribes, not just short-term cash-flow interests of specific tribes.[45] Allowing tribes to exact compensation that drives needed utility infrastructure and economic development away from tribal lands is not in the interest of any tribe.

Trust concepts and the statutory guidance that compensation be "just," consequently, support a standard that not only ensures fairness to tribes, but also that right-of-way holders and the public not be unfairly burdened because an unqualified consent requirement enables tribes to exact excessive compensation.

## IX. RELEVANT CASE LAW REJECTING "CORRIDOR" THEORY

Courts have rejected methods some tribes have sought to use to value energy rights-of-way, including the "pipeline corridor" methodology. In *Questar Southern Trails Pipeline v. 3.47 Acres of Land*, U.S.D.C. Cause No. CIV-02-10 BB/LFG (D.N.M.)(on appeal), United States District Judge Bruce Black of the District of New Mexico concluded that "No one in the real world uses the 'pipeline corridor' theory to value ranch or residential land." Based on that conclusion, Judge Black refused to allow testimony on the theory.[46]

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[44] *See Cheyenne-Arapaho Tribes of Okla. v. United States*, 966 F.2d 583, 591 (10th Cir. 1992), *cert. denied*, 113 S. Ct. 1642 (1993); *Woods Petroleum Co. v. U.S. Dep't of Interior*, 18 F.3d 854, 858 (10th Cir. 1994), *reaffirmed*, 47 F.3d 1032, 1038 (10th Cir.) (en banc), *cert. denied sub nom., Spotted Wolf v. Woods Petroleum Co.*, 116 S. Ct. 54 (1995) (requiring the BIA to look beyond "the short-term financial interest of the Indian lessors," recognizing that such an approach "could in the long run be harmful to the interests of Indian lessors.").

[45] *See Woods Petroleum Co. v. U.S. Dep't of Interior*, 18 F.3d at 858; *Yavapai-Prescott Indian Tribe v. Watt*, 707 F.2d 1072 (9th Cir.), *cert. denied*, 464 U.S. 1017 (1983),

[46] Memorandum Opinion Excluding Pipeline Corridor Theory at 2 (July 31, 2003). A copy of Judge Black's Opinion is attached as Exhibit G to this White Paper.

Similarly, United States District Judge B. Lynn Winmill of the District of Idaho found "pipeline corridor" evidence of value inadmissible in *Northwest Pipeline Corp. v. 95.02 Acres of Land*, U.S.D.C. Cause No. CV-01-628-E-BLW (D. Idaho, December 19, 2003). ("Project enhancement rule" precludes evidence of value created by the condemnor's use of the land, absent proof of a "true market" for land in the area for pipeline corridor uses).[47]

Tribes and tribal advocates also have posited "build around" theories of value, based on the total additional right-of-way and construction cost to the energy transporter to build around a reservation, and have sought a percentage of the energy transporters' total revenue as compensation. These are rooted in the leverage tribes have to impose a value and on notions of a right-of-way holder's supposed ability to pay. These theories typically involve unfounded policy pre-conceptions, including entirely inaccurate assumptions about the "profits" of energy transporters in a high commodity price environment and unproven assertions about historical rates of compensation for tribal rights-of-way. In any event, these theories do not soundly rest on rational, time-tested methods for determining market-based land values that are fair to both parties and to the consuming public.

## X. CONCLUSION AND RECOMMENDATIONS

Fair market valuation principles have long been used to determine the appropriate compensation to be paid for rights-of-way on federal public domain and federal reserved lands and on private lands. These principles should apply with equal force on lands held in trust by the United States for Indian tribes or other Native American groups and on lands of Indian tribes and groups that are subject to restrictions on alienation, such as certain Spanish and Mexican land grant lands held by New Mexico's Pueblos. Congress has embraced fair market principles in the Indian Land Consolidation Act. The Secretaries should recommend embracing those principles here. They are fair.

Other sovereigns, including the United States, accept FMV for rights-of-way acquired on their lands. However, if the Secretaries consider an alternative that tribes obtain a premium over FMV due to sovereignty considerations or for any other reason, that premium should be based on FMV, to assure an objective standard, and could be a reasonable multiple of FMV.

In the 1948 General Indian Right-of-Way Act, Congress specified compensation for rights-of-way be "just." *See* 25 U.S.C. § 325. That language makes plain that Congress cannot have intended that Indian tribes be authorized to impose unreasonable terms and conditions, including compensation requirements tens or hundreds of times fair market value, as a condition to their consent to the Secretary's

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[47] Copies of the *Northwest Pipeline* Order and Opinion are attached as Exhibit H to this White Paper.

grant of rights-of-way. Indian tribes should not be permitted to continue to use their strategically located reservations as a way to expropriate huge payments that lack any reasoned or logical relation to the fair market value of the lands involved. That excessive market power distorts energy market signals and, consequently, mis-allocates energy development resources. Tribes' requiring shorter term ROWs as a condition of their consent imposes still more excessive costs on consumers and diverts energy transportation resources to wasteful renewal negotiations.

This is particularly damaging with respect to right-of-way renewals where right-of-way holders have invested considerable sums of money in the construction or installation of energy products pipelines or electric transmission line infrastructure. As the Council of Energy Resources Tribes observed in their recent publication, "Assessing Rights-of-Way on Tribal Lands," p. 11 (August 2005):

> In terms of ROW rental fees, the increase in cost of circumventing the reservation may serve as a useful upper bound. A Tribe may have significantly more leverage during renewal of existing ROW agreements since the infrastructure typically is already in place and the marginal cost of relocating is likely to be quite high.

To prevent this over-reaching, the Secretaries should recommend that energy rights-of-way be granted in perpetuity or for the life of the infrastructure.

Without a reasonable standard for determining just and fair compensation and a procedure that provides finality and certainty, Indian tribes appear to be free, and some are prepared and advised, to extract compensation from right-of-way holders in amounts up to a dollar less than the cost of relocating those facilities around the Indian lands involved. *See* Assessing Rights-of-Way on Tribal Lands, p. 10 (advocating a "Cost Approach" in which ROW value is based on the "[t]otal cost of locating, appraising, negotiating for, and grading/preparing the ROW corridor" or "the assumption that a property is worth what it would cost a buyer to purchase a substitute site and modify it to provide the same utility as the property in question." Further, the Council of Energy Resource Tribes publication advocates:

> One prominent appraiser argues that price per acre is a "meaningless" measure of value. "If a corridor is wide enough to perform its connecting function, its width and area are of little importance." For this reason, *Tribes should only use land values as a starting point for valuing rights-of-way.*

*Id.* at 13 (citations omitted; emphasis added). This approach is completely unhinged from any reasonable notion of fair market value, and bears no relation to the value of the land.

For the reasons presented here, FAIR proposes the following legislative recommendations for the Secretaries' consideration in making their report to Congress:

1. Provide a standard for determining compensation, such as a reasonable multiple of fair market value, with FMV determined in accordance with the Federal Appraisal Standards for right-of-way grants, renewals and expansions. The standard may differ depending on whether tribal consent concerns a right-of-way for a grant, renewal or expansion. The Secretaries should consider the following solutions:

   a) Remove tribal consent authority and extend the status quo on non-tribal lands to tribal lands: "just compensation" under the Fifth Amendment of the U.S. Constitution as it has always existed for properties not on tribal lands. "Just compensation" should contemplate a term in perpetuity and an immediate right of entry onto the land; or,
   b) Maintain tribal consent authority and establish a standard of fair market value for a term of years when the parties cannot reach agreement; or,
   c) Maintain tribal consent authority and, when the parties cannot agree, establish a standard of fair market value-plus in perpetuity, where
      - "Plus" could mean an objective multiplier such as 3 or 5 times FMV; or,
      - "Plus" could mean subjective financial enhancements for geography, cultural sites, etc; or,
   d) Maintain tribal consent authority and establish a standard of fair market value-plus for a term of years for situations where the parties cannot reach agreement; and,
   e) Consent, once given, should extend for the life of the energy infrastructure project, until abandonment.

Establishment an ascertainable and fair standard benefits all parties. A standard benefits tribes allegedly being underpaid. A standard benefits companies overpaying.

2. Provide a procedure for implementing the objective, transparent, consistent and reliable standard described above, should the relevant energy infrastructure stakeholder and tribe reach an impasse. Such procedures can include referral of disputes to an appropriate forum in the federal court system, to the Federal Energy Regulatory Commission, to a special federal commission to be created, or to binding arbitration.

Please contact Nancy Ives, President of FAIR, nancy.ives@faircoalition.org, with any questions you may have. Thank you for your attention to this important matter.

# Exhibits To FAIR White Paper on Valuation

Exhibit A: Economic Analysis of Standards for ROW Fees on Tribal Trust Lands

Exhibit B: Uniform Appraisal Standards for Federal Land Acquisitions (2000) (Excerpts)

Exhibit C: Secretarial Order No. 3251, with Amendments

Exhibit D Secretarial Order No. 3258 and Related Secretarial Memorandum

Exhibit E: December 30, 2004 Department of Interior Policy on Alternative Methods of Valuation (An Excerpt of Exhibit D Provided Separately for Convenience)

Exhibit F: May 31, 2005 Memorandum from Brian M. Holley, MAI, DOI National Business Center, Appraisal Services Directorate, Chief Appraiser

Exhibit G: United States District Judge Bruce Black's Memorandum Opinion Excluding Pipeline Corridor Theory, *Questar Southern Trails Pipeline v. 3.47 Acres of Land*, U.S.D.C. Cause No. CIV-02-10 BB/LFG (D.N.M.) (on appeal)

Exhibit H: United States District Judge B. Lynn Winmill's Opinion and Order, *Northwest Pipeline Corp. v. 95.02 Acres of Land*, U.S.D.C. Cause No. CV-01-628-E-BLW (D. Idaho, December 19, 2003)

FAIR White Paper on Valuation: Exhibit A

Economic Analysis of Standards for ROW Fees on Tribal Trust Lands

## I. Introduction and Overview

An important economic goal of energy policy is to reduce the overall cost of meeting national energy needs: by economizing on resources used to meet those energy needs, we free up those resources to fund activities to benefit all Americans, including education, healthcare and basic scientific research. This paper explains how proposed reforms in rights of way (ROW) fees and negotiating procedures on tribal trust lands can help reduce the cost of meeting our nation's energy requirements. We discuss how these reforms can improve the incentive to invest in energy transportation infrastructure, reduce upward pressure on rates, and mitigate distortions in energy consumption decisions.

The remainder of this paper proceeds as follows. Section II provides some brief background on the energy transportation facilities that are the focus of the 1813 study– pipelines and transmission lines– and discusses how these facilities are impacted by ROW policy. Section III explains how ROW policy helps to control the cost of meeting U.S. infrastructure and energy needs on private lands. Section IV outlines how *de facto* ROW policy on tribal trust lands differs from that on U.S. private lands and discusses how these differences undermine the goal of meeting national energy needs at the lowest possible economic cost. Section V summarizes and concludes.

## II. Energy Transportation Providers and ROW Requirements

Pipelines transport gas and other petroleum products from producing areas to end users, while electric transmission lines carry power from generators to load. Both pipelines and transmission lines represent significant capital investments; these facilities often have declining average costs over the range of market demand. Under these circumstances, it can be most efficient (least cost) to have a single energy transportation provider serve a given market. Energy transportation facilities in this position are typically subject to rate regulation, which protects ratepayers from paying excessive rates for energy transportation services.

Long-established legal standards ensure that facilities subject to rate regulation have an opportunity to earn a competitive return on their invested capital. These standards help to ensure that funds continue to flow from financial markets into the energy transportation sector, providing companies with the capital necessary to build needed infrastructure, as well as to expand and maintain existing facilities.

ROW fees and negotiating standards are another aspect of public policy that can be critical to the economic viability of energy transportation providers and the communities they serve. ROW fees and negotiating standards are important to energy transporters because they must obtain permission from landowners to place their extremely costly physical assets on or in the ground. To obtain this permission, or land easement, transportation providers pay landowners for the right to access the land for new construction, facility upgrades, maintenance, and long-term service. ROW policy determines how much transportation providers must pay landowners for that right. Below, we discuss ROW policy on private and federal lands in the U.S. and compare its economic effects with the current ROW policy regime that prevails on tribal trust lands.

## III. ROW Policy on Private Lands in U.S.

### A. *Fair Market Value (FMV) Pricing Standard*

As explained in detail in the White Paper on Fair Market Valuation and Just Compensation for Rights of Way Across Tribal Lands (FMV White Paper), the FMV pricing standard is the basis for determining payments to landowners for easements on all private land and federal land in the United States. Under the FMV standard, landowners are made whole for any losses that they suffer as a proximate result of the energy transportation provider's activities on their land.[1] Such losses typically include reductions in the landowner's revenues (both actual and potential) arising from the transportation provider's activities.

From a public policy perspective, the FMV standard for ROW pricing is appropriate because it economizes on resources required to meet U.S. energy transportation needs, while ensuring that landowners are made whole for any reduction in the value of their property resulting from the easement. In contrast, if landowners were free to charge "whatever the transportation provider will bear," monopoly ROW fees charged to energy transporters could be passed on to the public in the form of distorted infrastructure investment decisions, upward pressure on rates, and inefficient energy consumption patterns. Distortions of this nature are typically a concern in markets where monopoly power is a problem. In fact, the U.S. government devotes significant resources to antitrust review and enforcement with the goal of preventing monopolistic practices and associated reductions in social welfare.[2]

The impact of an FMV-based pricing system for ROW can be illustrated with the following example. Suppose that a FERC-certificated pipeline seeks to connect a supply basin with a major population center. From an economic perspective it may be most efficient (least cost) for the pipeline to traverse a route that has been and will continue to be used for sheep grazing. With an easement for a buried pipe having little impact on sheep grazing activities, the value of the land would be relatively unimpaired by the easement. Hence, ROW prices based on FMV principles would be relatively low.

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[1] See FMV White Paper, Section IV.

[2] In some contexts, government policy tolerates monopoly pricing because the prospect of monopoly profits enhances innovative efficiency. For example, a company with a patent for a valuable invention is granted the ability to price the invention at monopoly levels because the availability of such profits provides an incentive to others to make similar innovations. The need for such incentives is much less significant for landowners in the path of energy transportation infrastructure. This is because the promise of monopoly fees for land usage does not increase the supply of available land. The profits that these landowners can earn– over and above what is necessary to compensate them for lost revenues and land value—produce market inefficiencies and reduce welfare, a result that has long been recognized in the economic literature.

On the other hand, if one rancher owns grazing land that covers all of the routes that the pipeline could traverse at reasonable cost, then that rancher, unconstrained by FMV standards, would have the incentive to charge the pipeline up to just less than the pipeline's build around costs for the easement. Ratepayers will suffer the ill effects of monopoly pricing regardless of whether the pipeline builds around the monopolist or simply accommodates the landowner's payment demands. This is because the monopolist's optimal payment demand will, in many cases, be just less than the cost of building around.[3]

If monopoly ROW fees only impact certain locations, the resulting regional variation in monopoly pricing of land will also distort energy users' decisions. Foreign and domestic energy sources that are relatively unaffected by monopolistic ROW pricing will appear increasingly competitive with other, cheaper, energy supplies that cannot avoid the imposition of monopoly land usage fees. As a result, energy users may find their demand skewed toward more costly energy resources that appear economical only because their transportation costs do not reflect monopoly ROW fees. Such distortions could also lead to increased dependence on foreign fuel supplies and suppliers.

The monopoly ROW fees discussed above are equivalent to a tax on the use of land. Like all taxes, this monopoly tax on the use of land distorts energy users' consumption decisions and reduces the welfare of society. Energy users subject to this monopoly land usage tax will pay too much for vital energy transportation facilities and demand fewer such facilities than would be the case under an FMV-based standard. As a result, too little energy transportation infrastructure will be built. With limited access to alternative energy supplies, energy users may be forced to consume the same commodity (e.g., gas) obtained from higher cost domestic regions or turn towards imports and/or substitute fuels (e.g., coal). In addition, these energy users may become more vulnerable to supply shortages and energy price spikes.

Current ROW pricing policy on private lands prevents landowners from imposing such wasteful land usage taxes on energy transporters and their ratepayers. However, under current law and Interior Department policy for tribal trust lands, this monopolistic pricing behavior would stand unchecked.

### B. *Upfront Easement Payments*

The current ROW policy package on U.S. private lands includes both the above-discussed easement prices based on FMV as well as the availability of perpetual easements for transportation providers. Because transportation providers typically pay private landowners one-time easement fees when they place their assets in or on the ground, there is much less opportunity for landowners to renegotiate easement terms

[3] Note that if an energy transportation provider could credibly demonstrate that its proposed project would be non-viable at less than build around cost, the landowner would have an incentive to take that constraint into account and adjust its payment demand accordingly.

during the economic life of the asset.[4] The upfront and well-defined nature of these easement payments is critical because energy transportation providers typically cannot move their facilities in or on the ground without incurring tremendous costs.

To see how an upfront ROW pricing standard promotes economic efficiency, suppose that instead of accepting a one-time upfront payment, a landowner had the power to renegotiate periodic renewal agreements with an incumbent infrastructure provider. Under these circumstances, the landowner would have an incentive to charge the provider up to its "shut down and build around" cost in each renewal period, all else equal. In addition, the landowner would have an incentive to reduce the periods between renewals as much as possible.

From a public policy perspective, continual renegotiations between landowners and incumbent providers with assets in the ground are likely to be extremely wasteful. One aspect of this waste is referred to in economic parlance as rent-seeking behavior. Landowners often have an enormous private incentive to pursue their goals through the negotiation process—the monetary value of the incumbent's build around (or work around) costs. However, the negotiation process itself has little or no socially beneficial impact. On the contrary, both parties to the negotiation consume valuable resources that could be spent more productively elsewhere, on building roads, schools, or additional energy infrastructure.

Of course, once the incumbent transportation provider becomes aware of the potential for repeated extraction of its profits, it will have the incentive to minimize its exposure to landowners' demands and/or seek out opportunities to relocate its vulnerable facilities. Unfortunately, moves of this kind represent an enormous diversion of resources that would be wholly unnecessary in a negotiating regime in which the landowner and the transportation provider had more equal bargaining power.

From this discussion, it should be clear that the current regime on U.S. private lands of eliminating opportunities for renegotiation when assets are already sunk in the ground helps mitigate the costs of meeting national needs for energy and associated infrastructure. These constraints on renewals reinforce the incentives created by FMV-based ROW pricing: they reduce landowners' incentives to sink resources in scheduling periodic renewals and to exploit the extractive opportunities that such renewals present. These constraints also reduce transportation providers' strong incentives to limit their exposure to this inequitable negotiation regime to the greatest extent possible.

## IV. ROW Policy Reform Required on Tribal Trust Lands

Currently, neither the FMV ROW pricing standard nor the requirement for perpetual easements is consistently applied on tribal trust lands.[5] Policymakers can reduce upward

[4] Note that when upfront fees are not charged, as in the case of the Bureau of Land Management (BLM), the yearly rental fee is based on FMV (See e.g. FMV White Paper, Section VIII.)

pressure on U.S. transportation infrastructure costs and energy prices by ensuring that easement pricing and negotiation standards applied on tribal trust lands are harmonized with the pricing and negotiation standards that prevail on all private and federal lands in the U.S.

## A. FMV ROW Pricing Standards Required at Geographic Pinch Points

If infrastructure providers could force landowners to compete with one another to provide access to their lands, the market could produce payments approximating the efficient FMV standard. However, in a number of regions of the U.S., tribes have a monopoly over the alternate routes that infrastructure providers could access at reasonable cost.

For example, infrastructure that connects the San Juan Basin to cities in Arizona and California must cross tribal trust lands; no reasonable cost alternate route exists. Similarly, it is our understanding that energy transportation facilities undertaken to connect San Diego with Los Angeles cannot avoid tribal trust lands without taking on the enormous cost of navigating over inhospitable terrain. Moreover, there is evidence to suggest that tribal trust land monopolies may be expanding as some tribes seek to acquire and incorporate into trust land parcels that could constitute future alternative routes around their current property.[6]

In the case where no feasible alternative routes exist, the market left to its own devices will not yield ROW prices based on FMV principles. Instead, owners of tribal trust lands will be able to extract up to one dollar below build around costs.[7] With enormous build around costs, the implied "constraint" on monopoly landowners' demands will not offer infrastructure providers or their ratepayers anything close to the compensatory, FMV outcome. The result will be higher energy transportation rates, which may significantly impact consumption decisions.

## B. Renewal Process for ROW on Tribal Trust Lands Should Be Constrained

In addition to the lack of an FMV-based pricing standard, it is our understanding that under existing regulations, it is uncertain as to whether a company can pay upfront for a perpetual easement on tribal trust lands.[8] As a result, even existing infrastructure projects that paid a figure consistent with compensatory value for their original easements can be "held up" in subsequent negotiations.[9] Such hold up can take many forms, as discussed

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[5] See FMV White Paper, Section V: "...BIA ignores the statutory language requiring that compensation be in an amount "the Secretary ...shall determine to be just" and disclaims any responsibility to determine FMV and approve rights-of-way for a FMV-based value..."

[6] See, e.g., Comments submitted by Sempra in this proceeding.

[7] Of course, an energy transportation provider might be able to secure lower ROW fees if it can credibly demonstrate that it will abandon a proposed infrastructure project at a given ROW price.

[8] It is our further understanding that tribal landowners often refuse to consent to perpetual easements for pipelines and electric transmission lines.

[9] From an economic perspective, the term "hold up" refers to a situation in which one party uses its superior bargaining power to extract concessions from another, often in the context of a negotiation. In the

in detail in the various comments submitted in this proceeding, including those provided by INGAA, EEI, and Sempra.

As noted above, the immediate effect of allowing tribes to behave opportunistically towards incumbent infrastructure providers is higher ROW costs for the facilities and their ratepayers. In the longer term, both tribes and incumbent energy providers have the incentive to expend significant resources on periodic agreement renegotiations that add little or no economic value. Moreover, infrastructure providers have the incentive to avoid new projects that involve traversing tribal trust lands, as well as to divert valuable resources towards investigating build around options in an effort to exit permanently from tribal trust lands.

## *C. ROW Approach on Tribal Trust Lands Undermines ROW Policy on Private Lands*

The *de facto* ROW policy on tribal trust lands is in direct conflict with several other aspects of national energy policy. First, it subverts state and federal regulation of public utility rates. As noted above, pipelines, transmission lines and other energy transportation providers are typically subject to rate regulation, which is intended to protect ratepayers from above-competitive pricing of energy transportation services. If a landowner is able to charge monopoly ROW prices to a utility, the utility has an opportunity to recover these costs by raising its customers' rates. Through this process, however, tribal landowners are able to undercut regulatory constraints on energy transportation rates.

In addition, ROW policy on tribal trust lands undermines ROW pricing policy on private lands. Private individuals have long been required to make their land available to public infrastructure projects such as pipelines and transmission lines at FMV-based prices. This requirement has an important public policy rationale: projects being built pursuant to the public good should not be subject to a wasteful monopoly tax. However, negotiators on tribal trust lands can take advantage of this constraint on all other landowners to extract rents from the very public works projects that the FMV-based pricing standard was intended to protect and encourage.

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current setting, once an energy transportation provider has sunk considerable resources on tribal trust land, the tribe has power emanating from its ability to control the transportation provider's continued ability to operate and serve its customers.

## V. Conclusion and Summary

By introducing FMV pricing standards on tribal trust lands and significantly constraining the easement renewal/renegotiation process, the U.S. will achieve three important goals.

> **First**, it will improve the investment incentives of energy transportation providers. These providers will have an increased motivation to build the right amount of infrastructure in the right places with the right resources at the right times, i.e., at the times at which such infrastructure is most needed.
>
> **Second,** the spread of objective, transparent, reliable and reasonable FMV-based pricing standards to tribal trust lands will remove significant uncertainty associated with transportation infrastructure projects. These proposed policy changes can reduce the needless risks that impact new energy transportation infrastructure projects as well as the threat of periodic renewals for easement terms of ever-declining duration. Both of these reductions in risk have the potential to increase the viability of energy transportation infrastructure projects.
>
> **Third**, these proposed policy changes can help moderate increases in consumer rates, both in the short term and in the longer term. With FMV-based pricing standards and upfront payments for longer-term easements based on facility lives, energy transportation rates will no longer reflect monopoly ROW fees. In the longer term, consumers will be able to meet their overall energy needs at lower cost, as transportation providers undertake projects that provide consumers with greater choice.

Moreover, the transition to FMV-based pricing and longer-term easements based facility lives can also provide long run benefits to tribes. Under the *de facto* ROW policy that exists on tribal trust lands, the looming threat of high costs, delays, uncertainty and extractive renewal policies indicate a hostile environment for business. Current policies signal to energy transportation providers and other firms not to build, invest, or create jobs on tribal trust lands. FMV-based pricing standards and longer term easements based on facility lives will contribute to an improved climate for investment on tribal trust land that can bring needed resources to these sovereign lands.

## FAIR White Paper on Valuation: Exhibit B

## Uniform Appraisal Standards for Federal Land Acquisitions

# Foreword

This is the fifth edition of the *Uniform Appraisal Standards for Federal Land Acquisitions*. The Standards were originally published in 1971 with the most recent revision published in 1992. The existing Standards have earned a prestigious position. They are frequently cited by Congress in legislation relating to the valuation of federal land acquisitions and have guided the appraisal process in these matters since their original issuance by the Interagency Land Acquisition Conference.

The Interagency Land Acquisition Conference, established on November 27, 1968, by invitation of the Attorney General, is a voluntary organization composed of representatives from the many federal agencies engaged in the acquisition of real estate for public uses. The Conference adopted and continues to adhere to several goals with respect to land acquisition, including the promulgation of uniform appraisal standards and guidelines for appraisal reports. The broad experience of the member representatives of the Interagency Land Acquisition Conference assures that the federal appraisal standards developed for land acquisitions are uniform, fair, and efficient. The Interagency Land Acquisition Conference is chaired by the Assistant Attorney General for the Environment and Natural Resources Division, Department of Justice. Its activities are conducted by *ad hoc* committees composed of member representatives.

The Interagency Land Acquisition Conference Executive is Virginia P. Butler, Chief of the Land Acquisition Section of the Environment and Natural Resources Division, Department of Justice. James D. Eaton, MAI, of the Appraisal Unit, Department of Justice, authored this 2000 revision of the *Uniform Appraisal Standards for Federal Land Acquisitions*. He was assisted in this effort by Appraisal Unit Chief Brian Holly, MAI; trial attorney Marc Gordon; and Ms. Butler. These Standards were submitted to the Appraisal Institute for editorial review and the Department of Justice gratefully acknowledges the editorial assistance of the Appraisal Institute in their preparation. While the vast majority of federal land acquisition is achieved through voluntary means, sometimes litigation is necessary. With this in mind, Mr. Eaton has done an admirable job of updating the case law, expanding the treatment of novel or difficult valuation questions, and recognizing the vast changes that have recently characterized the real estate appraisal profession.

The various departments and agencies of the Interagency Land Acquisition Conference commented upon a draft of these Standards. Their comments and suggestions were taken into account in a modified final revision that the Conference approved.

Under a cooperative agreement between the Appraisal Institute and the Department of Justice, the Appraisal Institute will publish this 2000 edition of the *Uniform Appraisal Standards for Federal Land Acquisitions*. Publication of these Standards will ensure that the "Yellow Book" is available in hard copy to all potential users. The Standards are also available on the Department of Justice's Internet Web site.

**Lois J. Schiffer, Chair**
**Interagency Land Acquisition Conference**
**Dated: December 20, 2000**

# Purpose

These Standards have been prepared for use by appraisers to promote uniformity in the appraisal of real property among the various agencies acquiring property on behalf of the United States. It should make no difference to the landowner, whose property is being acquired, which agency is acquiring the land, or what method of acquisition it uses.

Uniformity and fairness in the treatment of property owners are also the goals of the Uniform Relocation Assistance and Real Property Acquisition Policies Act of 1970, P.L. 91-646, as amended, 42 U.S.C §4601, et seq. Portions of this Act deal with the appraisal of real property and are cited and discussed herein in the appropriate sections. These Standards presume full compliance with the pertinent provisions of the Act.

The appraisal of property for purposes of direct voluntary purchase, exchange, or eminent domain by the United States presents unique problems not ordinarily encountered in appraisals for sale, tax, mortgage, rate-making, insurance, and other purposes. This results naturally from the fact that the method of appraisal, the elements and factors to be considered and the weight given them, and the standards of valuation are determined to a great extent by law. Therefore, the judgment or opinion of the individual appraiser should be governed by proper legal standards, whether land is being acquired by voluntary purchase, exchange, or condemnation.

These Standards have been prepared in recognition of the fact that the vast majority of federal land acquisitions are accomplished by voluntary means. However, the utmost objectivity, accuracy, and thoroughness of appraisals, upon which those acquisitions are based, is essential regardless of the government's method of acquisition. The federal appraisal standards are the same for voluntary acquisitions as they are for acquisitions by condemnation. Therefore, the purpose of these Standards is to set forth the general principles applicable to the appraisal of property for federal land acquisitions by both voluntary means and condemnation.

The rules stated herein are subject to modification under the varying circumstances of particular agency programs or cases.[1] Of course, the application of the general rules can reveal wide differences of opinion, some of which must ultimately be resolved in court. Because the amount of compensation to be paid to property owners when their property is acquired by the government for public use is a matter of constitutional law, appraisers are cautioned to confer with counsel for the acquiring agency on legal questions affecting the valuation and, if condemnation is instituted or appears necessary, with the representatives of the Department of Justice who will be charged with the responsibility of preparing the case for trial. In this manner, specific written legal instructions can resolve doubt about the proper method of valuation or the application of particular rules to specific factual situations.

Appraisers and other users should also recognize that these Standards may require modification in certain specific cases prompted by special legislation or court order, by stipulations made between an agency and a property owner in a voluntary acquisition, or by stipulations entered into between litigants in a condemnation action. Such modifications, however, should not be undertaken without specific written instructions from the acquiring agency or its legal counsel.

1. Many of the land acquisition agencies have adopted appraisal and/or review handbooks or manuals which, in some instances, modify these Standards to meet their specific acquisition programs. Examples of such manuals/handbooks include U.S. Fish and Wildlife Service (342 FW 1, *Appraisal Handbook*, 342 FW 2, *Appraisal Review Handbook*); U.S. Forest Service (*Manual* FSM 5410; *Handbook* FSH 5409); *U.S. Army Corps of Engineers Real Estate Engineer Regulations* (ER 405-1-12); *Bureau of Land Management Manual* (9310).

# Scope

These Standards will cover the following areas:

A. Data documentation and appraisal reporting standards
B. Legal basis for appraisal standards for federal land acquisitions
C. Standards for the review of appraisals
D. Standards for unique and miscellaneous appraisal problems

Section A of these Standards derives from generally accepted professional appraisal standards and appraisal reporting standards. However, these have occasionally been modified to meet the overriding standards created by federal law, as described in Section B of these Standards. The standards for appraisal report content and documentation presented in this section must be met. However, the appraisal report formatting presented here is merely recommended rather than mandatory.[2]

Section B of these Standards is based on federal case law, which is cited throughout the section. The U.S. Constitution provides that private property will not be taken and converted to public use by the government without payment to the landowner of just compensation. The federal courts have adopted the working rule that, in general, the just compensation due for the acquisition of property by the government is equivalent to the property's *market value*. It is, therefore, incumbent upon appraisers who make market value appraisals for federal land acquisitions to understand the federal case law relating to proper application of the appraisal process as applied to federal land acquisitions.

In addition to the case law that supports and, in some instances, dictates the standards set out in Section A, Section B includes a discussion of the legal standards established for treatment of many recurring valuation problems. Therefore, Section B of the Standards is intended for use not only by appraisers, but also by agency and Department of Justice attorneys whose legal practice includes matters relating to real estate valuation.

Section C of the Standards is derived from generally accepted appraisal review standards, as well as from federal regulations requiring such reviews. The purpose of Section C is to insure that appraisals used by the government in its land acquisitions have been

2. Nonetheless, appraisers should review their appraisal contracts or assignment letters in this regard. Some agencies may specify in their contracts/assignment letters that the use of Section A formatting is mandatory.

conducted in an unbiased, accurate, and thorough manner in accordance with these Standards and applicable law.

Section D addresses the proper treatment of specialized or unique but frequently encountered appraisal problems.

While these Standards aim both to encourage uniform approaches to appraisal problems and to prescribe requirements for adequate supporting data and other factual information used to develop market value estimates, the materials are not in any degree presented to limit the scope of appraisal investigations or to bias the independent judgment of value estimates of appraisers employed by federal agencies. Also, to insure maximum flexibility to agencies in accomplishing their program goals, provisions have been made, under certain circumstances, for the modification of the Section A "Data Documentation and Appraisal Reporting Standards." (See Section A, Introduction.)

# Policy

In acquiring real property, or any interest therein, it is United States' policy to impartially protect the interests of all concerned. The Fifth Amendment of the United States Constitution asserts: "nor shall private property be taken for public use, without just compensation." Since "the courts early adopted, and have retained, the concept of market value"[3] as the measure of just compensation, the United States, as a matter of general policy, bases its land acquisitions on market value appraisals: "[I]t is the duty of the state, in the conduct of the inquest by which the compensation is ascertained, to see that it is just, not merely to the individual whose property is taken, but to the public which is to pay for it."[4]

3. *United States v. Miller*, 317 U.S. 369, 374 (1943).

4. *Searl v. School District, Lake County*, 133 U.S. 553, 562 (1890); *Bauman v. Ross*, 167 U.S. 548, 574 (1897).

# B Legal Basis for Appraisal Standards for Federal Land Acquisitions

**B-1. Federal Law Controls.** Since the experience of many appraisers primarily involves non-public acquisition appraisals, or conducting appraisals under various state laws, it is particularly important that appraisers bear in mind that in federal acquisitions, because the meaning of *just compensation* is a matter of fundamental constitutional interpretation, questions with respect to compensation are to be resolved in accordance with federal rather than state law.[94] Because federal law differs in some important aspects from the law of some states, it is incumbent upon both the attorney and the appraiser to make certain that they understand the applicable federal law as it affects the appraisal process in the estimation of market value, which will generally be the basis for determining just compensation for property acquired by the United States for public purposes. While state law once controlled procedural matters, since the adoption in 1951 of Rule 71A, Federal Rules of Civil Procedure, procedural as well as substantive matters in federal condemnation cases are controlled by federal law.[95]

State law is sometimes referred to, though not necessarily followed, in resolving the nature of property rights acquired. The Supreme Court of the United States has stated that "[t]hough the meaning of 'property' . . . in the Fifth Amendment is a federal question, it will normally obtain its content by reference to local law."[96] It has been judicially made clear that "[t]his does not mean, however, that every local idiosyncrasy or artificiality in a state's concepts, or the incidents thereof, necessarily will be accepted."[97] It is also established that the United States may elect to acquire whatever interest it deems necessary whether or not the state recognizes the definition of the interest selected.[98]

**B-2. Market Value Criterion.** Under established law, the criterion for just compensation is the *market value* of the property taken. As stated by the U.S. Supreme Court:

> The United States has the authority to take private property for public use by eminent domain, but is obliged by the Fifth Amendment to provide "just compensation" to the owner thereof. "Just

94. *United States v. 93.970 Acres of Land*, 360 U.S. 328, 332-333 (1959); *United States v. Miller*, 317 U.S. 369, 380 (1943).
95. *Kirby Forest Industries, Inc. v. United States*, 467 U.S. 1, 3-4 (1984); *United States v. 93.970 Acres of Land*, 360 U.S. 328, 333, n.7 (1959).
96. *United States ex rel. T.V.A. v. Powelson*, 319 U.S. 266, 279 (1943).
97. *State of Nebraska v. United States*, 164 F.2d 866, 868 (8th Cir. 1947), cert. denied 334 U.S. 815.
98. *United States v. Little Lake Misere Land Company*, 412 U.S. 580, 604 (1973); *United States v. Certain Interests in Property in Champaign County, Ill.*, 271 F.2d 379, 384 (7th Cir. 1959), cert. denied 362 U.S. 974.

> Compensation," we have held, means in most cases the fair market value of the property on the date it is appropriated. "Under this standard, the owner is entitled to receive 'what a willing buyer would pay in cash to a willing seller' at the time of the taking."[99]

On a number of occasions, the Supreme Court has addressed the issue of market value, as the measure of just compensation, in federal condemnation cases. The following definition of market value has been adopted for use by appraisers in applying these Standards to their appraisals and reports prepared for federal land acquisitions:

> Market value is the amount in cash, or on terms reasonably equivalent to cash, for which in all probability the property would have sold on the effective date of the appraisal, after a reasonable exposure time on the open competitive market, from a willing and reasonably knowledgeable seller to a willing and reasonably knowledgeable buyer, with neither acting under any compulsion to buy or sell, giving due consideration to all available economic uses of the property at the time of the appraisal.

This definition is based on a compendium of Supreme Court decisions regarding the definition of market value for federal eminent domain purposes.[100] As with most definitions of market value, this one contains various implicit elements, some of which have "been hedged with certain refinements developed over the years in the interest of effectuating the constitutional guarantee" of just compensation.[101]

In ascertaining market value, consideration should be given to all matters that might be brought forward and reasonably be given substantial bargaining weight by persons of ordinary prudence, but no consideration whatever should be given to matters not affecting market value.[102] In developing the generally applied rule that market value is the measure of just compensation, the federal courts have employed variations of the term *market value*; as explained by the Supreme Court in *United States v. Miller*, 317 U.S. 369, 374 (1943) (internal citations omitted):

> The owner has been said to be entitled to the "value," the "market value," and the "fair market value" of what is taken. The term "fair" hardly adds anything to the phrase "market value" which denotes what "it fairly may be believed that a purchaser in fair market conditions would have given," or, more concisely, "market value fairly determined."

It is clear from these decisions that the adding of adjectives, such as *fair* or *cash* to the term *market value* does not alter its meaning for federal acquisition purposes.

The Supreme Court has cautioned that:

> strict adherence to the criterion of market value may involve elements which, though they affect such value, must in fairness be eliminated in a condemnation case, as where the formula is attempted to be applied as between an owner who may not want to part with his land because of its special adaptability to his own use, and a taker who needs the land because of its peculiar fitness for the taker's purposes. These elements must be disregarded by the fact finding body in arriving at "fair" market value.[103]

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99. *Kirby Forest Industries, Inc. v. United States*, 467 U.S. 1, 9-10 (1984) (citations omitted).

100. *Almota Farmers Elevator and Warehouse Co. v. United States*, 409 U.S. 470, 474 (1973); *Kerr v. South Park Commissioners*, 117 U.S. 379, 386-387 (1886); *United States v. Miller*, 317 U.S. 369, 374 (1943); *Kirby Forest Industries, Inc. v. United States*, 467 U.S. 1, 10 (1984); *McCoy v. Union Elevated R.R. Co.*, 247 U.S. 354, 359 (1918); *United States v. Reynolds*, 397 U.S. 14, 17 (1970).

101. *United States v. Reynolds*, 397 U.S. 14, 16 (1970).

102. *United States v. 50 Acres of Land*, 469 U.S. 24, 29 (1984).

103. *United States v. Miller*, 317 U.S. 369, 375, (1943). *See also United States v. Fuller*, 409 U.S. 488, 491 (1973).

Likewise, since market value is the test, no consideration should be given in the appraisal to any special value of the property to the owner not directly reflected in the market value.[104]

In this connection, the Supreme Court has noted that "[t]he value compensable under the Fifth Amendment, therefore, is only that value which is capable of transfer from owner to owner and thus of exchange for some equivalent. Its measure is the amount of that equivalent."[105] The Court goes on to state: "If exchanges of similar property have been frequent, the inference is strong that the equivalent arrived at by the haggling of the market would probably have been offered and accepted, and it is thus that the 'market price' becomes so important a standard of reference."[106] Accordingly, it is the *market price* which arises from the "haggling of the market" which is being sought. When price-controlled property is taken, the controlled price, being the only lawful market price, is the normal measure of just compensation,[107] as "The Fifth Amendment allows the owner only the fair market value of his property; it does not guarantee him a return on his investment."[108]

It is significant that the federal definition of market value is based on the presumption that the property, prior to the effective date of valuation, was on the open market for a reasonable length of time to find a buyer who was ready, willing, and able to consummate a purchase on the effective date of valuation. The federal courts have not attempted to define a *reasonable length of time,* probably in recognition of the fact that such length of time may vary dependent upon a myriad of factors, such as property type, market conditions, property location, and price range of property. Nor have the federal courts required that an estimate of market value be *linked* to a specified exposure time on the open market, only that it be *reasonable* under the circumstances. For that reason, appraisers should not link their estimates of market value made for federal acquisition purposes to a specific exposure time. To do so places a limiting condition on the estimate that is not required for federal land acquisition purposes, and one which may be found to be unacceptable by the federal courts.

The question of what constitutes reasonably knowledgeable buyers and sellers, within the context of market value, has been addressed. It has been found that *reasonably knowledgeable* does not require buyers and sellers to be all-knowing, but rather to have the knowledge possessed by the "typical 'willing buyer-willing seller'" in the marketplace: "The market from which a fair market value may be ascertained need not contain only legally trained (or advised) persons who fully investigate current land use regulations; ignorance of the law is every buyer's right."[109] Consideration should be given to "a relevant market made up of investors who are real but are speculating in whole or major part."[110] As the same court explained in a later appeal:

> The uncontroverted evidence of an active real estate market compels the conclusion that the typical 'willing buyer-willing seller' requirement of fair market value had been met; it would be inappropriate for a court to substitute its own judgment of value for that of the market. While an [appraiser] might be justified in adjusting the fair market value figure by discarding aberrational values based upon sales between related entities or fraudulent sales to widows and orphans, an [appraiser] may not discard an entire market as aberrational.[111]

104. *United States v. 50 Acres of Land,* 469 U.S. 24, 35 (1984); *United States v. 564.54 Acres of Land,* 441 U.S. 506, 511 (1979); *United States v. Miller,* 317 U.S. 369, 375 (1943).
105. *Kimball Laundry Co. v. United States,* 338 U.S. 1, 5 (1949).
106. Ibid., 6.
107. *United States v. Commodities Trading Corp.,* 339 U.S. 121, 124-125 (1950).
108. *United States ex rel. T.V.A. v. Powelson,* 319 U.S. 266, 285 (1943).
109. *Florida Rock Industries, Inc. v. United States,* 18 F.3d 1560, 1566, n.12 (Fed. Cir. 1994).
110. *Florida Rock Industries, Inc. v. United States,* 791 F.2d 893, 903 (Fed. Cir. 1986).
111. *Florida Rock Industries, Inc. v. United States,* 18 F.3d 1560, 1567 (Fed. Cir. 1994).

The Supreme Court has ruled that any alteration in the market value of the property being acquired that is attributable to the project for which it is being acquired must be disregarded.[112] This subject is discussed in detail in Section B-10. The market value which is sought is not merely theoretical or hypothetical; it represents, insofar as it is possible to estimate it, the actual selling price. As has been judicially declared: "where 'private property is taken for public use, and there is a market price prevailing at the time and place of the taking, that price is just compensation.'"[113]

Even though "[t]he Court has repeatedly held that just compensation normally is to be measured by 'the market value of the property at the time of the taking contemporaneously paid in money,'"[114] it has also recognized that deviation from this measure of just compensation has sometimes been required "'when market value has been too difficult to find, or when its application would result in manifest injustice to owner or public.'"[115] As explained by Justice Douglas:

> The Court in its construction of the constitutional provision has been careful not to reduce the concept of "just compensation" to a formula. The political ethics reflected in the Fifth Amendment reject confiscation as a measure of justice. But the Amendment does not contain any definite standards of fairness by which the measure of "just compensation" is to be determined. The Court in an endeavor to find working rules that will do substantial justice has adopted practical standards, including that of market value. But it has refused to make a fetish even of market value, since that may not be the best measure of value in some cases.[116]

This should not be construed to mean that in all instances in which highly similar comparable sales are unavailable, the courts will disavow the market value measure of compensation. As the Supreme Court explained:

> There may have been, for example, so few sales of similar property that we cannot predict with any assurance that the prices paid would have been repeated in the sale we postulate of the property taken. We then say that there is 'no market' for the property in question. But that does not put out of hand the bearing which the scattered sales may have on what an ordinary purchaser would have paid for the claimant's property. We simply must be wary that we give these sparse sales less weight than we accord 'market' price, and take into consideration those special circumstances in other sales which would not have affected our hypothetical buyer.[117]

The Court has also made it clear that "[t]he ascertainment of compensation is a judicial function, and no power exists in any other department of the government to declare what the compensation shall be or to prescribe any binding rule in that regard"[118] because the meaning of *just compensation* is a matter of fundamental constitutional interpretation, and the ability to make binding interpretations of the Constitution rests only with the United States Supreme Court.

In short, while the "Court has never attempted to prescribe a rigid rule for determining what is 'just compensation' under all circumstances and in all cases . . . market value has normally been accepted as a just standard."[119] Thus, these Standards are based on the premise that the compensation for federal land acquisitions will be measured by the

112. *United States v. Reynolds,* 397 U.S. 14, 16-17 (1970).

113. *United States v. Toronto, Hamilton & Buffalo Navigation Co.*, 338 U.S. 396, 404 (1949), citing *United States v. New River Collieries,* 262 U.S. 341, 344 (1923).

114. *United States v. 50 Acres of Land,* 469 U.S. 24, 29 (1984) (citations omitted).

115. Ibid.

116. *United States v. Cors,* 337 U.S. 325, 332 (1949) (citations omitted).

117. *United States v. Toronto, Hamilton & Buffalo Navigation Co.*, 338 U.S. 396, 402 (1949).

118. *United States v. New River Collieries,* 262 U.S. 341, 343-344 (1923).

119. *United States v. Commodities Trading Corp.*, 339 U.S. 121, 123 (1950).

relatively *objective working rule*[120] of market value as established by the Supreme Court over 100 years ago.[121] It is also for that reason that appraisers are instructed by these Standards to estimate the market value of property being acquired by the government, rather than to estimate the just compensation due for the property acquired. The determination of "just compensation" is beyond the scope of the appraiser's assignment, expertise, and authority. If the circumstances of a particular case render the market value measure "too difficult to find, or when its application would result in manifest injustice to owner or public,"[122] that determination will be made by the court in accordance with applicable law.

Buildings and improvements,[123] timber, crops, sand, gravel, minerals, oil, and so forth, in or upon the property are to be considered to the extent that they enhance the market value of the property as a whole. The total value of the property shall not be estimated by adding the values of such separate items to the value of the land, and the fact that the various items are in separate ownerships does not alter this rule. It must be remembered that it is the market value of the entire property that is the standard of valuation, and not the total of the money values of the separate items. This subject is discussed in greater detail in Section B-13 of these Standards. The mere possibility of the existence of minerals, oil, or gas is not sufficient to affect market value. Such a possibility can be given consideration only when there is sufficient probability of the presence of mineral, oil, or gas as to affect market value and when that probability would be given weight by a prudent person in bargaining.

Government-constructed buildings and improvements put on the property during the government's prior occupancy (e.g., when the government begins construction of the public improvement prior to the transfer of title and the effective date of the appraisal, or when the government made improvements as a prior lessee of the property) are often excluded from consideration in estimating market value, depending upon the specific facts of the case. Therefore, appraisers who encounter government-constructed improvements on the property to be appraised as of the effective date of the appraisal should request written instructions from the client agency or legal counsel on how the improvements should be treated.[124]

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120. *United States v. 564.54 Acres of Land,* 441 U.S. 506, 511 (1979).

121. E.g., *Boom Company v. Patterson,* 98 U.S. 403, 408 (1878).

122. *United States v. 50 Acres of Land,* 469 U.S. 24, 29 (1984).

123. Section 302(a) of P.L. 91-646, the Uniform Relocation Act (URA), approved January 2, 1971, 84 Stat. 1905, 42 U.S.C. §4652 provides:

> [n]otwithstanding any other provision of law, if the head of a federal agency acquires any interest in real property in any State, he shall acquire at least an equal interest in all buildings, structures, or other improvements located upon the real property so acquired and which he requires to be removed from such real property or which he determines will be adversely affected by the use to which such property will be put.

The appraiser should receive from the acquiring agency advice as to the requirements of such agency for the removal of buildings, structures and the identification of these which the head of the agency determines will be adversely affected by the proposed use of the property. However, appraisers should also recognize that such instructions may not be applicable if the case is referred to the Department of Justice for condemnation, because Section 102 of the Act provides:

> (a) The provisions of section 4651 of this title of the Act [relating to real property acquisition policy and practices] create no rights or liabilities and shall not affect the validity of any property acquisitions by purchase or condemnation.
>
> (b) Nothing in this Act shall be construed as creating in any condemnation proceedings brought under the power of eminent domain, any element of value or of damage not in existence immediately prior to January 2, 1971. 42 U.S.C. §4602.

124. In researching this issue, legal counsel may want to start their research by referring to the following cases: *Old Dominion Co. v. United States,* 269 U.S. 55, 65 (1925); *Searl v. School District, Lake County,* 133 U.S. 553, 562-565 (1890); *Washington Metropolitan Area Transit Authority v. One Parcel of Land,* 780 F.2d 467, 471 (4th Cir. 1986); *United States v. Delaware, Lackawana & Western Railroad Co.,* 264 F.2d 112, 116-117 (3rd Cir. 1959); *Bibb County, Georgia v. United States,* 249 F.2d 228, 230 (5th Cir. 1957), but see *United States v. Certain Space in Rand McNally Building,* 295 F.2d 381, 383-384 (7th Cir. 1961).

As a general rule, the property being acquired should be valued as of the time of acquisition, or as near that time as is possible.[125] When the appraisal is made after the taking, no consideration whatever should be given to physical changes, particularly improvements made by the condemnor, or changes in value occurring after the taking. Likewise, as discussed in Section B-10, no consideration should be given to or allowance made for enhancement or diminution in value of the property attributable to or resulting from the project or from the government's special need for the property, other than that due to physical deterioration within the reasonable control of the owner, whether such changes in value occur before or after the time of acquisition.

**B-3. Highest and Best Use.** Market value is to be determined with reference to the property's *highest and best use,* that is:

> The highest and most profitable use for which the property is adaptable and needed or likely to be needed in the reasonably near future. . . .[126]

Such use "is to be considered, not necessarily as the measure of value, but to the full extent that the prospect of demand for such use affects the market value while the property is privately held."[127]

"Ordinarily, the highest and best use for property sought to be condemned is the use to which it is subjected at the time of the taking. This is true because economic demands normally result in an owner's putting his land to the most advantageous use."[128] In the conduct of appraisals for federal land acquisition purposes, there is a presumption that the existing use of land is its highest and best use.[129] Therefore, when there is a claim that the highest and best use of a property is something other than the property's existing use, the burden of proving that different highest and best use is on the party making the claim.[130]

However, if the property is clearly adaptable to a use other than the existing use, its marketable potential for such use should be considered to the extent that potential affects market value.[131] But, market value cannot be predicated upon potential uses that are speculative and conjectural; as the Supreme Court has said:

> Elements affecting value that depend upon events or combinations of occurrences which, while within the realm of possibility, are not fairly shown to be reasonably probable should be excluded from consideration, for that would be to allow mere speculation and conjecture to become a guide for the ascertainment of value—a thing to be condemned in business transactions as well as in judicial ascertainment of truth.[132]

A proposed highest and best use requires a showing of reasonable probability that the land is both physically adaptable for such use **and** that there is a need or demand for such

125. That will generally be the date of the appraiser's last property inspection in voluntary acquisitions. In a declaration of taking case, the proper time of valuation is the date of filing the declaration of taking or the date of the government's entry into possession, whichever occurs first. *United States v. Dow,* 357 U.S. 17, 21-22 (1958). In a *straight* condemnation (without declaration of taking), the date of commencement of trial is used as the date of valuation. *See Kirby Forest Industries, Inc., v. United States,* 467 U.S. 1, 16-17 (1984), for a full discussion of the date of valuation question in a straight condemnation case.

126. *Olson v. United States,* 292 U.S. 246, 255 (1934). *See also Boom Company v. Patterson,* 98 U.S. 403, 408 (1878).

127. Ibid.

128. *United States v. Buhler,* 305 F.2d 319, 328 (5th Cir. 1962).

129. *United States v. L. E. Cooke Company, Inc.,* 991 F.2d 336, 341 (6th Cir. 1993); *United States v. 62.50 Acres of Land,* 953 F.2d 886, 890 (5th Cir. 1992); *United States v. 69.1 Acres of Land.,* 942 F.2d 290, 292 (4th Cir. 1991).

130. *United States v. 62.50 Acres of Land,* 953 F.2d 886, 890 (5th Cir. 1992); *Tennessee Gas Pipeline Co. v. 104 Acres of Land,* 780 F.Supp. 82, 86 (D.R.I. 1991).

131. *Olson v. United States,* 292 U.S. 246, 255 (1934).

132. Ibid., 257.

use in the reasonably near future; physical adaptability alone is insufficient.[133] "[O]bviously the more profitable operation must be allowed by law to be carried out on the premises."[134] (See Sections B-23, "Zoning and Permits" and D-6, "Zoning and Other Land Use Regulations.")

In no event may an appraisal be made on the basis of one use for the land while the improvements are valued on the basis a different, inconsistent use. (See A-14, "Analysis of Highest and Best Use"). Various parts of a single property may have different highest and best uses as long as these uses are not inconsistent (e.g., residential or commercial along road or highway frontage and agricultural use for the rear land).[135] These differences, however, may enter into the determination of the larger parcel, which is discussed in Section B-11. In no event is it proper that the different uses be valued independently and merely added together to derive a value for the whole property.[136]

Highest and best use cannot be predicated on a demand created solely by the project for which the property is acquired (e.g., rock quarry, when the only market is the highway project for which property was acquired.).[137] A proposed highest and best use cannot be the use for which the government is acquiring the property (e.g., missile test range, habitat conservation, airfield, park), unless there is a prospect and competitive demand for that use by others than the government:[138]

> The Supreme Court has recognized the existence of a 'principle which excludes enhancement of value resulting from the government's special or extraordinary demand for the property.'. . . .The focal point of the 'special or extraordinary' standard is that values resulting from the urgency or uniqueness of the government's need for the property or from the uniqueness of the use to which the property will be put do not reflect what a willing buyer would pay to a willing seller. . . . [I]t is clear that government projects may render property valuable for a unique purpose. Value for such a purpose, if considered, would cause 'the market to be an unfair indication of value,' because there is no market apart from the government's demand.[139]

Likewise, "[t]he benefit a real estate development produces for a community or the amenity contribution provided by a planned project (i.e., the public space in a park-like area) is not considered in the appraiser's analysis of highest and best use. Highest and best use is driven by economic considerations and market forces, not by public interest."[140] Therefore, "a non-economic highest and best use is not a proper basis for the estimate of market value [thus] a highest and best use of conservation, preservation, or other use that

133. Ibid., 256; *United States v. 27.93 Acres of Land*, 924 F.2d 506, 512 (3rd Cir. 1991); *United States v. 33.90 Acres of Land*, 709 F.2d 1012, 1014-1015 (5th Cir. 1983); *United States v. 158.24 Acres of Land*, 696 F.2d 559, 563 (8th Cir. 1982); *United States v. 77,819.10 Acres of Land*, 647 F.2d 104, 110 (10th Cir. 1981).

134. *United States v. Meadow Brook Club*, 259 F.2d 41, 45 (2nd Cir. 1958), cert. denied, 358 U.S. 921.

135. *United States v. 179.26 Acres of Land*, 644 F.2d 367, 371 (10th Cir. 1981); *United States v. 320.0 Acres of Land*, 605 F.2d 762, 817 n.124 (5th Cir. 1979); *Eagle Lake Improvement Co. v. United States*, 160 F.2d 182, 184 (5th Cir. 1947), cert. denied, 332 U.S. 762; *United States v. Carrol*, 304 F.2d 300, 306 (4th Cir. 1962).

136. *United States v. 91.90 Acres of Land*, 586 F.2d 79, 87 (8th Cir. 1978); cert. denied, 441 U.S. 944 (1979); *Morton Butler Timber Co. v. United States*, 91 F.2d 884, 888 (6th Cir. 1937); *United States v. Jaramillo*, 190 F.2d 300, 302 (10th Cir. 1951); *United States v. Certain Parcels of Land in Rapides Parish, La.*, 149 F.2d 81, 82 (5th Cir. 1945).

137. *United States v. Cors*, 337 U.S. 325, 333 (1949); *United States v. 320.0 Acres of Land*, 605 F.2d 762, 811 n. 107 (5th Cir. 1979); *United States v. 46,672.96 Acres of Land*, 521 F.2d 13, 15, 16 (10th Cir. 1975); *J. A. Tobin Construction Co. v. United States*, 343 F.2d 422, 423 (10th Cir. 1965), cert. denied, 382 U.S. 830; *United States v. 158.76 Acres of Land*, 298 F.2d 559, 560 (2nd Cir. 1962).

138. *United States v. Chandler-Dunbar Co.*, 229 U.S. 53, 80-81 (1913); *United States v. 320.0 Acres of Land*, 605 F.2d 762, 783 n.26, 811 n.107 (5th Cir. 1979); *United States v. 46,672.96 Acres of Land*, 521 F.2d 13, 15-16 (10th Cir. 1975).

139. *United States v. Weyerhaeuser Co.*, 538 F.2d 1363, 1366, 1367 (9th Cir. 1976), cert. denied, 429 U.S. 929 (1976) (internal citations omitted).

140. *The Appraisal of Real Estate*, 11th ed. (Chicago: Appraisal Institute, 1996), 298 n.1.

requires the property to be withheld from economic production in perpetuity, is not a valid use upon which to estimate market value."[141]

The Department of Justice's "view is that an appraisal premised on a highest and best use of 'preservation,' 'conservation,' 'natural lands' and the like is not an appraisal of 'fair market value' and is unacceptable for both direct purchase and eminent domain acquisitions. That view is largely based on the principles of eminent domain law from which we conclude that a non-economic use is not a proper basis for assessing fair market value, that a value premised on a highest and best use of 'preservation' or the like does not represent a 'market' value, and certainly does not represent a 'fair' value."[142] Therefore, the Department of Justice will not approve any appraisal report for federal acquisition purposes wherein the value estimate is based upon an uneconomic highest and best use. Nor will it approve any appraisal report that incorporates a definition of highest and best use that includes the concept of non-economic uses. (See A-14, "Analysis of Highest and Best Use.")

When determining the highest and best use of land riparian to navigable water, there are special considerations that must be taken into account. See discussion in Section B-14.

Because the highest and best use is a most important consideration in estimating market value, it must be dealt with specifically in appraisal reports. Many things must be considered in determining the highest and best use of property and each potential use must be analyzed in terms of its physical possibility, legal permissibility, financial feasibility, and its degree of profitability. That use which meets the first three tests and is the most profitable use (i.e., results in the highest value) is the property's highest and best use.

Important practical applications of highest and best use estimates arise in connection with partial acquisitions, such as flowage, conservation, clearance or other types of easements. The value of the remainder, after a partial acquisition, is governed largely by its highest and best use. If, for example, what was essentially farmland before the acquisition has become lakefront property having a highest and best use for recreational home sites, the important principle of offsetting special benefits discussed in Section B-12, might become applicable. However, if the acquisition causes the remainder property to have a less valuable highest and best use, the difference between the values of the property before and after the acquisition will reflect both the diminution in the value of the remainder resulting from the acquisition as well as the value of the land or property interest actually acquired. This is more fully discussed in Section B-11 of these Standards.

Concerning partial acquisitions, the appraiser must consider any material change in the intensity of use within a highest and best use classification: for example, when a balanced farm in the before position becomes an unbalanced farm in the after position because of the partial acquisition by the government.[143] The highest and best use classification of an agricultural farm would cover both positions. However, the two intensities of that use, a balanced versus an unbalanced farm, would identify the need to carefully re-analyze the comparative ratings of each of the comparable sales in the after position, or even the need to use different comparable sales in the after position than were used before the government's acquisition.

141. Interagency Land Acquisition Conference, "Position Paper: On the issue whether a noneconomic highest and best use can be a proper basis for the estimate of market value" (Washington D.C., 1995).

142. William J. Kollins, "Presentation on Issues Raised by the 'Public Interest Value' Concept: Views of the Department of Justice" (Paper delivered at the Annual Meeting of the American Society of Farm Managers and Rural Appraisers, Reno, NV, November 11, 1994), 4. *See also*, William J. Kollins, "Public Interest Value," *United States Attorney's Bulletin* (February 2000): 47-53.

143. For example, in the before position the farm may have a balanced ratio of supporting outbuildings to service the land area in the farm, whereas in the after position, because of the reduced land area of the farm, the outbuildings may constitute an over-improvement and thus contribute less value, because of the lessened land area to be served.

compensable damage.[290] However, appraisers must take care in this regard to avoid consideration of what are merely consequential, or noncompensable, damages.[291]

As noted above, in conducting appraisals for the government, market rent is estimated without regard to any subsidiary interests into which the property may have been divided. However, client agencies may, on occasion, expand the scope of an appraiser's assignment to include consideration of the values of such subsidiary interests, so as to provide the agency with additional information that will facilitate its acquisition/negotiation activities. Compensation due to the owners of such subsidiary interests will vary depending on the nature and extent of the government's acquisition and the specific terms and conditions under which the subsidiary interest is held.

**B-20. Easements.** An easement can generally be described as an interest in land of another entitling the owner of that interest to a limited use of the land in which it exists, or a right to preclude specified uses in the easement area by others. An easement is an interest less than the fee estate, with the landowner retaining full dominion over the realty subject only to the easement; the landowner may make any use of the realty that does not interfere with the easement holder's reasonable use of the easement and is not specifically excluded by the terms of the easement. Federal acquisitions involve a wide variety of easement types ranging from the traditional to the exotic; they include, for example, road, pipeline, electric transmission line, levee, flowage, clearance, avigation, scenic, conservation, tunnel, sewer line, and safety zone easements.

In making an appraisal in conjunction with an easement acquisition,[292] it is imperative that the appraiser have a clear understanding of the specific terms of the easement involved, as the burden on the land upon which the easement is imposed (the servient estate) and the concomitant impact on the value of the affected land will vary according to the character of the easement.[293] (For example, there is no such thing as a generic road easement or a generic scenic easement.[294]) Also, full consideration should be given to and due allowance made for the rights remaining in the owner.[295]

Every easement acquisition is a partial acquisition leaving a remainder estate in the owner. This is true even where the entire ownership is impressed with the easement: because an easement is less than the fee, there is a remainder estate in the land within the easement. If the easement is impressed upon less than the full area of the larger parcel, the portion of the parcel outside the easement is also a remainder. Federal courts have long held that the appropriate measure of compensation in a partial acquisition is the difference between the value of the whole parcel before the acquisition and the value of the remainder after the acquisition.[296] The courts accordingly have held this to be the proper measure

290. Ibid.

291. Ibid. 701. See also discussion in Section B-15, "Noncompensability of Consequential Damages."

292. The first part of this Section will deal with appraisals made in conjunction with easement acquisitions. Subsequent portions will deal with the appraisal of existing easements taken or extinguished by the government's acquisition of the servient estate, and the appraisal of land encumbered by an easement.

293. "The valuation of an easement upon the basis of its destructive impact upon other uses of the servient fee is a universally accepted method of determining its worth." *United States v. Virginia Electric Co.*, 365 U.S. 624, 630 (1961).

294. For this reason, it is essential that the client agency provide the appraiser with a written description of the *estate to be taken* when an easement is to be acquired.

295. Where only an easement is acquired, the full fee value of the land within the easement is not necessarily a proper measure of diminution in value since the rights remaining in the owners may be very substantial. *See United States v. An Easement and Right-of-Way Over Two Strips of Land*, 284 F. Supp. 71, 73 (W.D. Ky. 1968).

296. See Section B-11. Because easement acquisitions are partial acquisitions, the rules on severance damages and offsetting of benefits apply.

of compensation in easement acquisitions.[297] If only the strip subject to the easement is valued, this violates the rule that "comparing the fair market value of the *entire* tract affected by the taking before and after the taking . . . states the correct measure of value in federal court condemnation."[298]

For some types of easements, such as those acquired for electric, telephone, fibre optics, cable lines and pipelines, there may be an established going rate per pole, per line-mile, per rod, and the like. In appraising a similar type of easement for government acquisition, the appraisal must not be based upon such going rates but must be based upon the usual before and after appraisal method.[299]

Although the before and after method of valuation is required by these Standards when the government acquires easements (because it measures what the owner has lost, not what the government has gained), use of the before and after method of valuation is not required when the government sells an easement interest. Agencies are, therefore, free to consider the value of the easement to the acquirer as well as the diminution to the government's property by reason of the encumbrance.

Easements may be permanent or temporary. An example of the latter is the temporary construction easement. The appropriate measure of value for the acquisition of a temporary easement is the rental value for the term of the easement, adjusted as may be appropriate for the rights of use, if any, reserved to the owner. See Section D-10 of these Standards for a fuller discussion of this point.

The foregoing discussion pertains to appraisals made for easement acquisitions. A quite different though related matter is the proper measure of value for a third party appurtenant easement that is acquired or extinguished as an incident of the government's acquisition of the servient estate (e.g., fee acquisition of property through which an easement of access connects a third party's parcel to the highway). The third-party easement owner has a separate estate that must be separately appraised.[300] In such cases, the easement owner is not limited to the value of the easement acquired, but is entitled to the value diminution of the property served by the easement.[301] Accordingly, two appraisal assignments are required; a before and after appraisal of the easement interest and the property it serves (the before appraisal including the easement interest and the land it serves and the after appraisal excluding those interests acquired by the government) and a second appraisal assignment covering the land being acquired, as encumbered by the easement.[302] This second appraisal would also require a before and after appraisal if only a portion of this larger parcel is to be acquired.[303]

297. *United States v. Virginia Electric Co.*, 365 U.S. 624, 632 (1961); *United States v. 8.41 Acres of Land*, 680 F.2d 388, 392 (5th Cir. 1982); *United States v. 38.60 Acres of Land*, 625 F.2d 196, 198-199 (8th Cir. 1980); *Transwestern Pipeline Co. v. O'Brien*, 418 F.2d 15, 21 (5th Cir. 1969).

298. *Transwestern Pipeline Co. v. O'Brien*, 418 F.2d 15, 21 (5th Cir. 1969) (emphasis added).

299. *United States v. 8.41 Acres of Land*, 680 F.2d 388, 392 (5th Cir. 1982).

300. This is an exception to the *unit rule* discussed in Section B-13, and is reasonable because the owner of the easement has a different larger parcel (the easement together with the land which it serves) than does the owner of the land encumbered with the easement.

301. *United States v. Grizzard*, 219 U.S. 180, 184-185 (1911); *United States v. 57.09 Acres of Land*, 706 F.2d 280, 281 (9th Cir. 1983).

302. *Boston Chamber of Commerce v. Boston*, 217 U.S. 189, 195 (1910); *United States v. 79.20 Acres of Land*, 710 F.2d 1352, 1354-1355 (8th Cir. 1983).

303. For a fuller discussion of this methodology, see J. D. Eaton, *Real Estate Valuation in Litigation*, 2nd ed. (Chicago: Appraisal Institute, 1995), 365-368.

**FAIR White Paper on Valuation: Exhibit C**

**Secretarial Order No. 3251, with Amendments**

# United States Department of the Interior

OFFICE OF THE SECRETARY
Washington, D.C. 20240

ORDER NO. 3251

SIGNATURE DATE: November 12, 2003

Subject: Consolidation of the Department=s Real Estate Appraisal Functions

Sec. 1 **Purpose**. This Order authorizes the consolidation of the Department=s real estate appraisal functions into the National Business Center (NBC) within the Office of the Secretary. The consolidation will ensure appraiser independence, accountability, high standards, appropriate training, and oversight of Departmental appraisal functions.

Sec. 2 **Authority**. This Order is issued in accordance with the authority provided by Section 2 of Reorganization Plan No. 3 of 1950 (64 Stat. 1262), as amended.

Sec. 3 **Establishment of the Office and Transfer of Functions**.

a. The Office of Appraisal Services (Office) is hereby established in the NBC and is headed by the Assistant Director, Appraisal Services. The Assistant Director is the Department=s Chief Appraiser. The headquarters of the Office is located in Washington, D.C., with regional and field offices located throughout the United States. Each region is headed by a Regional Supervisory Appraiser, reporting to the Assistant Director. Field offices will report to the region.

b. Real estate appraisal functions are hereby transferred from all bureaus and offices (with the exception of the Office of the Special Trustee for American Indians) to the Office.

c. Appraisers from the following bureaus are to be transferred to the new office: Bureau of Land Management; National Park Service; U.S. Fish and Wildlife Service; and the Bureau of Reclamation.

Sec. 4 **Appraisal Standards**. All real estate appraisals must be performed pursuant to the Uniform Appraisal Standards for Federal Land Acquisitions or the Uniform Standards of Professional Appraisal Practice.

Sec. 5 **Delegation**. The authority of the Assistant Secretary - Policy, Management and Budget to carry out the real estate appraisal functions is delegated to the Director, NBC. This authority is further delegated to the Assistant Director, Appraisal Services.

Sec. 6 **Implementation**. The Assistant Secretary - Policy, Management and Budget is responsible for ensuring implementation of this Order, including the appropriate transfer of personnel, funds, facilities, programs, records, and property.

Sec. 7 **Expiration Date**. This Order is effective immediately. It will remain in effect until its provisions are converted to the Departmental Manual, or until it is amended, superseded or revoked, whichever comes first. In the absence of any of the foregoing actions, the provisions of this Order will terminate and be considered obsolete on October 31, 2004.

/s/ Gale A. Norton
Secretary of the Interior

SO#3251 11/12/03

THE SECRETARY OF THE INTERIOR
WASHINGTON

ORDER NO. 3251, Amendment No. 1 ***(Amended material italicized)***

SIGNATURE DATE: October 22, 2004

Subject: Consolidation of the Department's Real Estate Appraisal Functions

Sec. 1 **Purpose**. This Order authorizes the consolidation of the Department's real estate appraisal functions into the National Business Center (NBC) within the Office of the Secretary. The consolidation will ensure appraiser independence, accountability, high standards, appropriate training, and oversight of Departmental appraisal functions.

Sec. 2 **Authority**. This Order is issued in accordance with the authority provided by Section 2 of Reorganization Plan No. 3 of 1950 (64 Stat. 1262), as amended.

Sec. 3 **Establishment of the Office and Transfer of Functions.**

a. The ***Appraisal Services Directorate*** is hereby established in the NBC and is headed by the ***Associate Director, Appraisal Services Directorate***. The ***Associate Director*** is the Department's Chief Appraiser. The headquarters of the ***Directorate*** is located in Washington, D.C., with regional and field offices located throughout the United States. Each region is headed by a Regional Supervisory Appraiser, reporting to the ***Associate Director***. Field offices will report to the region.

b. Real estate appraisal functions are hereby transferred from all bureaus and offices (with the exception of the Office of the Special Trustee for American Indians) to the Office.

c. Appraisers from the following bureaus are to be transferred to the new office: Bureau of Land Management; National Park Service; U.S. Fish and Wildlife Service; and the Bureau of Reclamation.

Sec. 4 **Appraisal Standards**. All real estate appraisals must be performed pursuant to the Uniform Appraisal Standards for Federal Land Acquisitions or the Uniform Standards of Professional Appraisal Practice.

Sec. 5 **Delegation**. The authority of the Assistant Secretary - Policy, Management and Budget to carry out the real estate appraisal functions is delegated to the Director, NBC. This authority is further delegated to the Assistant Director, Appraisal Services.

Sec. 6 **Implementation**. The Assistant Secretary - Policy, Management and Budget is responsible for ensuring implementation of this Order, including the appropriate transfer of personnel, funds, facilities, programs, records, and property.

Sec. 7 **Expiration Date**. This Order is effective immediately. It will remain in effect until its provisions are converted to the Departmental Manual, or until it is amended, superseded or revoked, whichever comes first. In the absence of any of the foregoing actions, the provisions of this Order will terminate and be considered obsolete on ***October 31, 2005***.

/s/ Gale A. Norton
Secretary of the Interior

SO#3251A1 10/22/04
Replaces SO#3251 11/12/03

ORDER NO. 3251, Amendment No. 2 ***(Amended material italicized)***

SIGNATURE DATE: October 28, 2005

Subject: Consolidation of the Department's Real Estate Appraisal Functions

Sec. 1 **Purpose**. This Order authorizes the consolidation of the Department's real estate appraisal functions into the National Business Center (NBC) within the Office of the Secretary. The consolidation will ensure appraiser independence, accountability, high standards, appropriate training, and oversight of Departmental appraisal functions.

Sec. 2 **Authority**. This Order is issued in accordance with the authority provided by Section 2 of Reorganization Plan No. 3 of 1950 (64 Stat. 1262), as amended.

Sec. 3 **Establishment of the Office and Transfer of Functions**.

a. The Appraisal Services Directorate is hereby established in the NBC and is headed by the Associate Director, Appraisal Services Directorate. The Associate Director is the Department's Chief Appraiser. The headquarters of the Directorate is located in Washington, D.C., with regional and field offices located throughout the United States. Each region is headed by a Regional Supervisory Appraiser, reporting to the Associate Director. Field offices will report to the region.

b. Real estate appraisal functions are hereby transferred from all bureaus and offices (with the exception of the Office of the Special Trustee for American Indians) to the Office.

c. Appraisers from the following bureaus are to be transferred to the new office: Bureau of Land Management; National Park Service; U.S. Fish and Wildlife Service; and the Bureau of Reclamation.

Sec. 4 **Appraisal Standards**. All real estate appraisals must be performed pursuant to the Uniform Appraisal Standards for Federal Land Acquisitions or the Uniform Standards of Professional Appraisal Practice.

Sec. 5 **Delegation**. The authority of the Assistant Secretary - Policy, Management and Budget to carry out the real estate appraisal functions is delegated to the Director, NBC. This authority is further delegated to the Assistant Director, Appraisal Services.

Sec. 6 **Implementation**. The Assistant Secretary - Policy, Management and Budget is responsible for ensuring implementation of this Order, including the appropriate transfer of personnel, funds, facilities, programs, records, and property.

Sec. 7 **Expiration Date**. This Order is effective immediately. It will remain in effect until its provisions are converted to the Departmental Manual, or until it is amended, superseded or revoked, whichever comes first. In the absence of any of the foregoing actions, the provisions of this Order will terminate and be considered obsolete on ***May 31, 2006***.

/s/ Gale A. Norton
Secretary of the Interior

SO#3251A2 10/28/05
Replaces SO#3251A1 10/22/04
Replaces SO#3251 11/12/03

FAIR White Paper on Valuation: Exhibit D

Secretarial Order No. 3258 and Related Secretarial Memorandum

THE SECRETARY OF THE INTERIOR

WASHINGTON

ORDER NO: 3258

Subject: Policy Guidance Concerning Land Valuation and Legislative Exchanges

Sec. 1 **Purpose.** This Order provides policy for land valuation issues, real property appraisals, and legislative land exchanges.

Sec. 2 **Background.** During the past year, the Department has taken significant steps to ensure that land transactions are conducted with integrity and earn public confidence. These steps include implementing reforms to improve the management of real property appraisals, establishing the Appraisal Services Directorate, and issuing the Land Transaction Principles. This Order provides the following: (a) a policy on alternative methods of valuation (AMV) that addresses the need to comport with nationally applicable appraisal standards; (b) a policy on appraisals prepared for third (*i.e.*, non-Federal) parties; and (c) a policy on legislative exchanges that reinforces existing Departmental guidance and further provides for a Departmental determination on how to review such proposals internally to ensure appropriate coordination and decision making. The legislative exchange policy also underscores the importance of adhering to applicable appraisal standards in developing applicable legislative provisions.

Sec. 3 **Authority.** The policy in this Order is being issued in accordance with the Uniform Appraisal Standards for Federal Land Acquisitions and the Uniform Standards of Professional Appraisal Practice.

Sec. 4 **Policy.**

a. <u>Alternative Methods of Valuation</u>.

(1) All real property appraisals performed by the Department shall conform to nationally recognized appraisal standards (*i.e.*, the Uniform Appraisal Standards for Federal Land Acquisitions and the Uniform Standards of Professional Appraisal Practice, as applicable). Accordingly, the use of public interest value, contingent valuation, habitat equivalency analysis, and any other AMV in appraisals is expressly prohibited.

(2) If Congress directs the Department to utilize AMV other than or in addition to an appraisal in a specific transaction, the Department shall (a) expressly describe the AMV applied; (b) using the assistance of the Appraisal Services Directorate (ASD), explain how the AMV differ from appraisal methods applied under UASFLA or USPAP; and (c) upon Congressional direction, provide this material to the appropriate committees prior to or after completion of the transaction, in accordance with such direction.

(3) Requirement for Congressional Authorization or Notification.

(a) If the Department proposes to utilize AMV other than or in addition to an appraisal in a specific transaction that requires Congressional authorization, the Department shall expressly describe to the appropriate committees of Congress the AMV applied and, using the assistance of the ASD, explain how they differ from appraisal methods applied under UASFLA or USPAP.

(b) If the Department proposes to utilize AMV other than or in addition to an appraisal in a specific transaction that does not require Congressional authorization, the Department shall notify the appropriate committees of Congress and the Office of the Inspector General prior to the completion of the transaction and, upon Congressional direction, explain, using the assistance of the ASD, to the appropriate committees how the AMV differ from appraisal methods applied under UASFLA or USPAP.

(4) The Associate Director, ASD, has overall authority and responsibility to ensure the effective implementation of this policy, in coordination with the Office of the Special Trustee for American Indians (OST), as applicable, and the Office of Congressional and Legislative Affairs (OCL).

b. Appraisals Prepared for Third (*i.e.*, non-Federal) Parties.

(1) Appraisals prepared for third (*i.e.*, non-Federal) parties may assist in achieving mutually beneficial outcomes for the Department and the proponent. The Department of the Interior, however, is not obligated to review land transaction proposals supported by such appraisals that do not comport with its land management missions, priorities, and plans.

(2) Upon bureau request, the Department, acting through the ASD or the OST, as applicable, shall review a third party appraisal if: (a) the third party consults with ASD or OST prior to the initiation of the appraisal on the scope of work and the selection of the appraiser, and agree that ASD or OST, as applicable, is both the client for and an intended user of the appraisal; (b) a senior bureau or Departmental manager (*i.e.*, Senior Executive Service level in the field or headquarters, as applicable) has transmitted the appraisal with a determination that the land transaction proposal supported by the appraisal comports with applicable missions, priorities, and plans; and (c) ASD or OST, as applicable, has determined that the appraisal was prepared by a certified appraiser and meets applicable appraisal standards.

(3) ASD or OST review of an appraisal does not create an expectation that such appraisal will be approved.

(4) In cases where an appraisal is reviewed by ASD or OST, a second appraisal may be required. If so, ASD or OST shall conduct or oversee that appraisal, which shall be performed in accordance with procedures determined by ASD or OST, as applicable.

(5) The Associate Director, ASD, has overall authority and responsibility to ensure the implementation of this policy in coordination with OST, as applicable, and the OCL.

c. Legislative Exchanges.

(1) All officials and employees of the Department shall adhere to 461 DM 1, which addresses requests for information, drafting, or other assistance regarding legislation from sources outside the Department, and specifically requires coordination with the Legislative Counsel in OCL.

(2) Similar coordination with the OCL shall occur on legislative exchange proposals initiated by any entity, official, or employee of the Department.

(3) The OCL shall determine the appropriate means for the review of each legislative exchange proposal, including the involvement of appropriate policy officials of other offices (*e.g.*, the ASD or the OST as appropriate, and the Solicitor).

(4) Appropriate documentation shall support the key provisions of all legislative exchange proposals.

(5) All appraisals used in legislative exchanges shall conform to nationally recognized appraisal standards (*i.e.*, the Uniform Appraisal Standards for Federal Land Acquisitions and the Uniform Standards of Professional Appraisal Practice, as applicable). When the Department proposes the application of alternative methods of valuation other than or in addition to an appraisal for a legislative exchange, it shall expressly describe the alternative methods of valuation and explain how they differ from methods utilized in an appraisal consistent with nationally recognized appraisal standards (*i.e.*, the Uniform Appraisal Standards for Federal Land Acquisitions and the Uniform Standards of Professional Appraisal Practice, as applicable).

(6) The Director, OCL, has overall authority and responsibility to ensure the effective implementation of this policy, in coordination with the Associate Director, ASD, as applicable.

**Sec. 5 Expiration Date.** This Order is effective immediately. It will remain in effect until its provisions are converted to the Departmental Manual or until it is amended, superseded, or revoked, whichever occurs first. In the absence of any of the foregoing actions, the provisions of this Order will terminate and be considered obsolete on July 30, 2006.

Gale A. Norton
Secretary of the Interior

Date: DEC 30 2004

THE SECRETARY OF THE INTERIOR

WASHINGTON

DEC 30 2004

Memorandum

To: Deputy Secretary
Solicitor
Assistant Secretaries
Special Trustee for American Indians
Inspector General
Director, Bureau of Indian Affairs
Director, Bureau of Land Management
Director, Fish and Wildlife Service
Director, National Park Service
Commissioner, Bureau of Reclamation

From: Secretary Gale A. Norton

Subject: Policy Guidance Concerning Legislative Exchanges and Land Valuation Issues

Over the past year, the Department has taken significant steps to ensure that land transactions are conducted with integrity and earn public confidence. I am especially pleased with the implementation of our initiative to reform the management of real estate appraisals and by the formulation of Land Transaction Principles to guide our activities. In order to build on our progress, further actions are required as outlined in this memorandum and the attached policy guidance.

Last summer, I asked the Land Transaction Group (LTWG) to develop recommendations concerning land transactions such as exchanges that the Department initiates or negotiates which require Congressional ratification. In addition, the LTWG has been developing recommendations concerning significant issues related to the appraisal process. The attachment outlines policies that I am establishing for Department-wide implementation concerning: (a) alternative methods of valuation; (b) third party (*i.e.*, non-Federal) appraisals; and (c) legislative exchanges.

The policy on alternative methods of valuation addresses the need to comport with nationally applicable appraisal standards, noting that the use of methods other than or in addition to market value appraisals must be clearly described and differentiated from recognized market value appraisals. This is essential since these appraisal standards do not allow for applying such alternatives to determine market value.

The policy on the use of third party (*i.e.*, non-Federal) appraisals states that such an appraisal will not be accepted for review unless: the proponent has consulted with the Appraisal Services Directorate (National Business Center) regarding the project's scope of work and other key considerations; a senior agency or Departmental manager determines that the transaction it supports comports with applicable land management missions, priorities, and plans; and the appraisal is prepared by a certified appraiser in accordance with applicable professional appraisal standards. The appraisal must also undergo appropriate review by the Appraisal Services Directorate before it may be used to execute a transaction.

The policy on legislative exchanges reinforces existing Departmental guidance, but further provides for a Departmental determination on how to review such proposals internally to ensure appropriate coordination and decision making. It also underscores the importance of adhering to applicable appraisal standards in developing applicable legislative provisions.

I am directing you to disseminate this guidance to appropriate personnel including program and field managers as well as to outside parties, and to ensure its incorporation in pertinent bureau or office guidance documents.

Attachments

# POLICY ON ALTERNATIVE METHODS OF VALUATION

## Background

The market value of properties is determined through appraisals conducted pursuant to nationally recognized appraisal standards, specifically the Uniform Appraisal Standards for Federal Land Acquisitions (UASFLA) or the Uniform Standards of Professional Appraisal Practice (USPAP). In recent years, some have asserted that non-market factors (*e.g.*, scenery, wildlife habitat, and conserved open space) also deserve consideration when transactions are negotiated. Policy guidance is needed to clarify the distinction between market value appraisals and alternative methods of valuation (AMV) employed to assess non-market factors.

In recent years, AMV have been advanced by those who assert that common measures of market value are unduly limiting. AMV are often advocated by proponents of specific exchanges or acquisitions to support the application of a premium above a property's appraised value or, incorrectly, as a proxy for market value. This occurs most often in cases of land use conflicts involving government regulation, where AMV are suggested as a basis for negotiating solutions to decision-making impasses.

Appraisal standards state that in conducting analyses of market value, the highest and best use of a property to be appraised must be an economic use. Accordingly, non-market factors cannot be considered in such analyses. Nonetheless, bureaus and other parties to transactions may be tempted to apply AMV to appraisals, especially when it proves difficult to meet requirements mandating "equal value" exchanges (which generally apply to all Interior agencies) or when they encounter other obstacles in negotiations. This has resulted in appraisals that do not conform to recognized appraisal standards. There are instances in which Congress directs bureaus to analyze and consider non-market factors or other "public interest" considerations when completing a transaction, or in which the Department itself proposes to do so, as a means of resolving land-based conflicts and advancing a broader public policy. Regardless, when AMV are used, *they must be clearly distinguished from appraisals.*

## Policy

1. All real property appraisals performed by the Department shall conform to nationally recognized appraisal standards (*i.e.*, the Uniform Appraisal Standards for Federal Land Acquisitions and the Uniform Standards of Professional Appraisal Practice, as applicable). Accordingly, the use of public interest value, contingent valuation, habitat equivalency analysis, and any other AMV in appraisals is expressly prohibited.

2. If Congress directs the Department to utilize AMV other than or in addition to an appraisal in a specific transaction, the Department shall (a) expressly describe the AMV applied; (b) using the assistance of the Appraisal Services Directorate (ASD), explain how the AMV differ from appraisal methods applied under UASFLA or USPAP; and (c) upon Congressional direction, provide this material to the appropriate committees prior to or after completion of the transaction, in accordance with such direction.

3. (a) If the Department proposes to utilize AMV other than or in addition to an appraisal in a specific transaction that requires Congressional authorization, the Department shall expressly describe to the appropriate committees of Congress the AMV applied and, using the assistance of the ASD, explain how they differ from appraisal methods applied under UASFLA or USPAP.

   (b) If the Department proposes to utilize AMV other than or in addition to an appraisal in a specific transaction that does not require Congressional authorization, the Department shall notify the appropriate committees of Congress and the Office of the Inspector General prior to the completion of the transaction and, upon Congressional direction, explain, using the assistance of the ASD, to the appropriate committees how the AMV differ from appraisal methods applied under UASFLA or USPAP.

4. The Associate Director, ASD, has overall authority and responsibility to ensure the effective implementation of this policy, in coordination with the Office of the Special Trustee for American Indians (OST), as applicable, and the Office of Congressional and Legislative Affairs (OCL).

## POLICY ON APPRAISALS PREPARED FOR THIRD PARTIES

Background

Appraisals prepared for third (*i.e.*, non-Federal) parties may assist in achieving conservation and land tenure adjustment objectives. This assistance may help provide mutually beneficial outcomes for the Department and its partners, including state and local agencies, private non-profit organizations, corporations, private entities, and individuals. Applicable partnership activities include land transactions such as exchanges and sales as well as full fee and less-than-fee purchases. The following policy provides direction regarding the use of third (*i.e.*, non-Federal) appraisals.

In many instances, the non-Federal party directly obtains an appraisal without any involvement from the pertinent bureau. Such third party appraisals have sometimes either been prepared by unqualified appraisers, failed to meet Federal appraisal standards, or insufficiently addressed all of the issues involved in the transaction. Substandard appraisals may seriously impact appraiser independence, undermine the integrity of transactions, and lead to antagonism between bureaus and proponents, especially when a transaction has significant external stakeholder support. Substandard appraisals ordered by non-Federal parties for a proposed transaction with the Department of the Interior have long been identified as a problem in reviews by the Office of Inspector General. The Department is now establishing a policy to ensure that its transactions are above reproach.

Policy

1. Appraisals prepared for third (*i.e.*, non-Federal) parties may assist in achieving mutually beneficial outcomes for the Department and the proponent. The Department of the Interior, however, is not obligated to review land transaction proposals supported by such appraisals that do not comport with its land management missions, priorities, and plans.

2. Upon bureau request, the Department, acting through the ASD or the OST, as applicable, shall review a third party appraisal if: (a) the third party consults with ASD or OST prior to the initiation of the appraisal on the scope of work and the selection of the appraiser, and agree that ASD or OST, as applicable, is both the client for and an intended user of the appraisal; (b) a senior bureau or Departmental manager (*i.e.*, Senior Executive Service level in the field or headquarters, as applicable) has transmitted the appraisal with a determination that the land transaction proposal supported by the appraisal comports with applicable missions, priorities, and plans; and (c) ASD or OST, as applicable, has determined that the appraisal was prepared by a certified appraiser and meets applicable appraisal standards.

3. ASD or OST review of an appraisal does not create an expectation that such appraisal will be approved.

4. In cases where an appraisal is reviewed by ASD or OST, a second appraisal may be required. If so, ASD or OST shall conduct or oversee that appraisal, which shall be performed in accordance with procedures determined by ASD or OST, as applicable.

5. The Associate Director, ASD, has overall authority and responsibility to ensure the implementation of this policy in coordination with OST, as applicable, and the OCL.

# POLICY ON LEGISLATIVE EXCHANGES

## Background

Legislative exchanges may resolve difficult land tenure adjustment issues, and thus provide beneficial outcomes to taxpayers, agencies, non-Federal units of government, and property owners affected by Federal activities. These exchanges, however, involve the Department in sensitive negotiations with potentially broad or precedent-setting implications. Accordingly, policy guidance is needed to clarify the roles and responsibilities of officials and employees.

Legislation is required to authorize land exchanges in two broad instances: (a) all interstate exchanges; and (b) exchanges directed by Congress which include provisions exempting agencies from one or more mandates that might otherwise apply, such as FLPMA land use planning requirements, NEPA, or requirements for appraisals. Additionally, a legislative exchange may be proposed even when no additional authority is required. Although most legislative exchanges address BLM lands, legislation has also been enacted concerning NPS and FWS lands.

Legislative exchanges are often proposed by Members of Congress without Departmental involvement in the development or drafting stages. In such cases, the Department's legislative review process is used to solicit internal comments and ultimately to recommend a Departmental or Administration position. In addition, the Departmental Manual (461 DM 1) requires bureaus or offices "receiving a request for information, drafting, or other assistance regarding the consideration or preparation of legislation, other than appropriations legislation, from sources outside the Department" to notify the Legislative Counsel. The Legislative Counsel is designated to work with the bureau or office to develop the draft legislation and ensure internal review prior to transmittal to Congress. In some cases, however, Interior involvement is as follows: (a) a Member of Congress requests a bureau to help draft an exchange proposal; or (b) bureaus draft exchange legislation on their own for discussion with a Member or Member's staff. These latter instances are addressed in the following policy.

## Policy

1. All officials and employees of the Department must adhere to 461 DM 1, which addresses requests for information, drafting, or other assistance regarding legislation from sources outside the Department, and specifically requires coordination with the Office of Congressional and Legislative Affairs (OCL), acting through the Legislative Counsel.

2. Similar coordination with the OCL shall occur on legislative exchange proposals initiated by any entity, official, or employee of the Department.

3. OCL shall determine the appropriate means for the review of each legislative exchange proposal, including the involvement of appropriate policy officials of other offices (*e.g.*, the Appraisal Services Directorate (ASD) of the National Business Center or the Office of the Special Trustee for American Indians, as applicable, and the Solicitor).

4. All legislative exchange proposals must be supported by appropriate documentation that supports key provisions.

5. All appraisals used in legislative exchanges shall conform to nationally recognized appraisal standards (*i.e.*, the Uniform Appraisal Standards for Federal Land Acquisitions and the Uniform Standards of Professional Appraisal Practice, as applicable). When the Department proposes the application of alternative methods of valuation other than or in addition to an appraisal for a legislative exchange, it shall expressly describe the alternative methods of valuation and explain how they differ from methods utilized in an appraisal consistent with nationally recognized appraisal standards (*i.e.*, the Uniform Appraisal Standards for Federal Land Acquisitions and the Uniform Standards of Professional Appraisal Practice, as applicable).

6. The Director, OCL, has overall authority and responsibility to ensure the effective implementation of this policy, in coordination with the Associate Director, ASD, as applicable.

FAIR White Paper on Valuation: Exhibit E

December 30, 2004 Department of Interior Policy on Alternative Methods of Valuation (An Excerpt from Exhibit D Provided Separately for Convenience)

## POLICY ON ALTERNATIVE METHODS OF VALUATION

Background

The market value of properties is determined through appraisals conducted pursuant to nationally recognized appraisal standards, specifically the Uniform Appraisal Standards for Federal Land Acquisitions (UASFLA) or the Uniform Standards of Professional Appraisal Practice (USPAP). In recent years, some have asserted that non-market factors (*e.g.*, scenery, wildlife habitat, and conserved open space) also deserve consideration when transactions are negotiated. Policy guidance is needed to clarify the distinction between market value appraisals and alternative methods of valuation (AMV) employed to assess non-market factors.

In recent years, AMV have been advanced by those who assert that common measures of market value are unduly limiting. AMV are often advocated by proponents of specific exchanges or acquisitions to support the application of a premium above a property's appraised value or, incorrectly, as a proxy for market value. This occurs most often in cases of land use conflicts involving government regulation, where AMV are suggested as a basis for negotiating solutions to decision-making impasses.

Appraisal standards state that in conducting analyses of market value, the highest and best use of a property to be appraised must be an economic use. Accordingly, non-market factors cannot be considered in such analyses. Nonetheless, bureaus and other parties to transactions may be tempted to apply AMV to appraisals, especially when it proves difficult to meet requirements mandating "equal value" exchanges (which generally apply to all Interior agencies) or when they encounter other obstacles in negotiations. This has resulted in appraisals that do not conform to recognized appraisal standards. There are instances in which Congress directs bureaus to analyze and consider non-market factors or other "public interest" considerations when completing a transaction, or in which the Department itself proposes to do so, as a means of resolving land-based conflicts and advancing a broader public policy. Regardless, when AMV are used, *they must be clearly distinguished from appraisals*.

Policy

1. All real property appraisals performed by the Department shall conform to nationally recognized appraisal standards (*i.e.*, the Uniform Appraisal Standards for Federal Land Acquisitions and the Uniform Standards of Professional Appraisal Practice, as applicable). Accordingly, the use of public interest value, contingent valuation, habitat equivalency analysis, and any other AMV in appraisals is expressly prohibited.

2. If Congress directs the Department to utilize AMV other than or in addition to an appraisal in a specific transaction, the Department shall (a) expressly describe the AMV applied; (b) using the assistance of the Appraisal Services Directorate (ASD), explain how the AMV differ from appraisal methods applied under UASFLA or USPAP; and (c) upon Congressional direction, provide this material to the appropriate committees prior to or after completion of the transaction, in accordance with such direction.

3. (a) If the Department proposes to utilize AMV other than or in addition to an appraisal in a specific transaction that requires Congressional authorization, the Department shall expressly describe to the appropriate committees of Congress the AMV applied and, using the assistance of the ASD, explain how they differ from appraisal methods applied under UASFLA or USPAP.

   (b) If the Department proposes to utilize AMV other than or in addition to an appraisal in a specific transaction that does not require Congressional authorization, the Department shall notify the appropriate committees of Congress and the Office of the Inspector General prior to the completion of the transaction and, upon Congressional direction, explain, using the assistance of the ASD, to the appropriate committees how the AMV differ from appraisal methods applied under UASFLA or USPAP.

4. The Associate Director, ASD, has overall authority and responsibility to ensure the effective implementation of this policy, in coordination with the Office of the Special Trustee for American Indians (OST), as applicable, and the Office of Congressional and Legislative Affairs (OCL).

FAIR White Paper on Valuation: Exhibit F

May 31, 2005 Memorandum from Brian M. Holley, MAI, DOE National Business Center, Appraisal Services Directorate, Chief Appraiser

# United States Department of the Interior

NATIONAL BUSINESS CENTER
APPRAISAL SERVICES DIRECTORATE
Office of the Chief Appraiser

U.S. Department of the Interior
NBC
National Business Center

Memorandum

To: OST-OAS Regional Appraisers

From: Brian M. Holly Brian M. Holly
Chief Appraiser
National Business Center

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Date: May 31, 2005

Subject: Appraisal Methodology for Rights of Way Grants across Individual Indian Lands

Issue: The purpose of this memorandum is to implement a consistent rights-of-way valuation policy for OST-OAS. Part 169 of Title 25 of the Code of Federal Regulations addresses the procedures terms and conditions under which rights of way over and across tribal land, individually owned land and government owned land may be granted. The following sections identify considerations which impact the proper appraisal of these rights of way easements.

Consideration for Right-of-Way Grants: Consideration for any right of way granted or renewed under this part 169 shall be not less than but not limited to the fair market value of the rights granted, plus severance damages, if any, to the remaining estate. The secretary shall obtain and advise the landowners of the appraisal information to assist them (the landowner or landowners) in negotiations for a right of way or renewal.
25 CFR 169.12

Tenure of Approved Right of Way Grants: All rights of way granted under the regulations in this part 169 shall be in the nature of easements for the periods stated in the conveyance instrument. 25 CFR 169.18

Renewal of Right of Way Grants: On or before the expiration date of any right of way heretofore or hereafter granted for a limited term of years, an application may be submitted for a renewal of the grant...The Secretary may with the consent required by 169.3 may thereupon extend the grant for a like term of years, upon the payment of consideration as set forth in 169.12. 25 CFR 169.19

Oil and Gas Pipelines: Rights of way granted under aforesaid Act of March 11, 1904, as amended, for oil and gas pipelines, pumping stations or tank sites shall not extend beyond a term of 20 years and may be extended for another period of not to exceed 20 years following the procedures set out in 169.19 of this part. 25 CFR 169.25

Power Projects: A right of way granted under the said Act of March 4, 1911, as amended, shall be limited to a term not exceeding 50 years from the date of the issuance of such grant. 25 CFR 169.27

There are three points when an appraisal may be required concerning these rights of way:

1. At the time the right of way is initially established.
2. At the time the right of way is expanded
3. At the time of renewal.

These appraisals are further complicated by the nature of the easements themselves which are limited in term to 20 years in the case of oil and gas pipelines or 50 years for electrical transmission lines. The nature of these transactions then is very different from the right of way easements found in the private sector which are generally in perpetuity.

The purpose of this policy is to provide specific guidance concerning the appraisal methodology to be followed in the appraisal of these rights of way.

Policy

All right of way appraisals prepared by the Office of Appraisal Services – Office of the Special trustee for American Indians (OAS) will be completed in accordance with Section B-20 of the *Uniform Appraisal Standards for Federal Land Acquisitions.* Specific provisions of this section state:

> "In making an appraisal with an easement acquisition, it is imperative that the appraiser have a clear understanding of the specific terms of the estate involved, as the burden on the land upon which the easement is imposed (the servient estate) and the concomitant impact on the value of the affected land will vary according to the character of the easement. Also, full consideration should be given to and due allowance made for the rights remaining in the owner.
>
> Every easement acquisition is a partial acquisition leaving a remainder estate in the owner... If the easement is impressed upon less than the full area of the larger parcel, the portion of the parcel outside the easement is also a remainder. Federal courts have long held that the appropriate measure of compensation in a partial acquisition is the difference between the value of the whole parcel before the acquisition and the value of the remainder after the acquisition."

These fundamental principals apply in the case of right of way easements across individual Indian lands.

In the case of new easements, the appraiser must consider all of the factors related to the specific terms of the easement estate and measure the impact on the value of the remainder. These impacts may be physical or legal in nature depending on the specific terms of the easement involved. A before and after approach as described in Section B-20 of the *Uniform Appraisal Standards for Federal Land Acquisitions* will result in proper consideration of the issues. The appraiser must be aware that the regulations permit consideration of damages to the remainder only and any special benefits are not to be considered in the analysis. Finally, great care must be taken to ensure that the analysis accounts for the fact that these easements are for a specific term of years. This is different from right of way easements typically found in the private market which are in perpetuity. This is a critical factor which must be addressed in the appraisal.

An appraisal prepared for an expansion of an existing easement must also be prepared in accordance with Section B-20. Specifically, if an additional easement is being acquired for a second pipeline adjacent to the first easement then the appraisal must consider the property encumbered by the first easement in the before valuation and then the property encumbered by both easements in the after valuation. Again, consideration must be made of all factors regarding the terms of the easements including the length of the term and the burdens imposed on the remaining land.

Finally, appraisals of easement renewals (as permitted under the existing regulations) must also use the before and after appraisal methodology. The appraiser is considering the situation which exists at the termination of the initial easement. At that point, the easement is extinguished and the property reverts to the owner. These appraisals should be carried out in the same manner that an appraisal of a new easement would be completed.

This policy will remain in effect until rescinded by action of the Chief Appraiser, U.S. Department of the Interior.

Signed

Brian M. Holly

Brian M. Holly, MAI
Chief Appraiser

## United States Department of the Interior
NATIONAL BUSINESS CENTER
APPRAISAL SERVICES DIRECTORATE
Office of the Chief Appraiser

Memorandum
To: OST-OAS Regional. Appraisers
From: Brian M. Holly
Chief Appraiser
National Business Center

Date: May 31, 2005
Subject: Appraisal Methodology for Rights of Way Grants across Individual Indian Lands

Issue: The purpose of this memorandum is to implement a consistent rights-of-way valuation policy for OST-OAS. Part 169 of Title 25 of the Code of Federal Regulations addresses the procedures terms and conditions under which rights of way over and across tribal land, individually owned land and government owned land may be granted. The following sections identify considerations which impact the proper appraisal of these rights of way easements.

Consideration for Right-of-Way Grants: Consideration for any right of way granted or renewed under this part 169 shall be not less than but not limited to the fair market value of the rights granted, plus severance damages, if any, to the remaining estate. The secretary shall obtain and advise the landowners of the appraisal information to assist them (the landowner or landowners) in negotiations for a right of way or renewal, 25 CFR 169.12

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Power Projects: A right of way granted under the said Act of March 4, 1911, as amended, shall be limited to a term not exceeding 50 years from the date of the issuance of such grant. 25 CFR 169.27

There are three points when an appraisal may be required concerning these rights of way:

1. At the time the right of way is initially established.

2. At the time the right of way is expanded.

3. At the time of renewal.

These appraisals are further complicated by the nature of the easements themselves which are limited in term to 20 years in the case of oil and gas pipelines or 50 years for electrical transmission lines. The nature *of* these transactions then is very different from the right of way easements found in the private sector which are generally in perpetuity.

The purpose of this policy is to provide specific guidance concerning the appraisal methodology to be followed in the appraisal of these rights of way.

Policy

All right of way appraisals prepared by the Office of Appraisal Services-Office of the Special Trustee for American Indians (OAS) will be completed in accordance with Section B-20 of the *(Uniform Appraisal Standards for Federal Land Acquisitions.* Specific provisions of this section state:
"In making an appraisal with an easement acquisition, it is imperative that the appraiser have a clear understanding of the specific terms of the estate involved, as the burden on the land upon which the easement is imposed (the servient estate) and the concomitant impact on the value of the affected land will vary according to the character of the easement. Also, full consideration should be given to and due allowance made for the rights remaining in the owner.

Every easement acquisition is a partial acquisition leaving a remainder estate in the owner... If the easement is impressed upon less than the full area of the larger parcel, the portion of the parcel outside the easement is also a remainder. Federal courts have long held that the appropriate measure of compensation in a partial acquisition is the difference between the value of the whole parcel before the acquisition and the value of the remainder after the acquisition."

These fundamental principals apply in the case of right of way easements across individual Indian lands.

In the case of new easements, the appraiser must consider all of the factors related to the specific terms of the easement estate and measure the impact on the value of the remainder. These impacts may be physical or legal in nature depending on the specific terms of the easement involved. A before and after approach as described in Section B-20 of the *Uniform Appraisal Standards for Federal Land Acquisitions* will result in proper consideration of the issues. The appraiser must be aware that the regulations permit consideration of damages to the remainder only and any special benefits are not to be considered in the analysis. Finally, great care must be taken to ensure that the analysis accounts for the fact that, these easements are for a specific term of years. This is different from right of way easements typically found in the private market which are in perpetuity. This is a critical factor which must be addressed in the appraisal.

An appraisal prepared for an expansion of an existing easement must also be prepared in accordance with Section 6-20. Specifically, if an additional easement is being acquired for a second pipeline adjacent to the first easement then the appraisal must consider the property encumbered by the first easement in the before valuation and then the property encumbered by both easements in the after valuation. Again, consideration must be made of all factors regarding the terms of the easements including the length of the term and the burdens imposed on the remaining land.

Finally, appraisals of easement renewals (as permitted under the existing regulations) must also use the before and after appraisal methodology. The appraiser is considering the situation which exists at the termination of the initial easement. At that point, the easement is extinguished and the property reverts to the owner. These appraisals should be carried out in the same manner that an appraisal of a new easement would be completed.

This policy will remain in effect until rescinded by action of the Chief Appraiser, U.S. Department of the interior.

Signed

Brian M. Holly, MAI
Chief Appraiser

The appraiser will determine damages to subservient property due to the imposition of the right of way easement and this impact rate will be extracted from the market. The preferred method is by determining the relationship of comparable sales of land unaffected by an easement to land affected by an easement. The next step is to make a term adjustment to account for the duration of the easement less than perpetuity. The appraiser is referred to Real Estate Valuation in Litigation, Second Edition, Chapter 16, Easements. The calculation, of the reversionary value of the easement is not a mandatory step in performing valuations of temporary/term easements. If the reversionary value is applied, a terminal capitalization rate shall be estimated and supported by the market.

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FAIR White Paper on Valuation: Exhibit G

United States District Judge Bruce Black's Memorandum Opinion Excluding Pipeline Corridor Theory, *Questar Southern Trails Pipeline v. 3.47 Acres of Land*, U.S.D.C. Cause No. CIV-02-10 BB/LFG (D.N.M.) (on appeal)

IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF NEW MEXICO

QUESTAR SOUTHERN TRAILS PIPELINE COMPANY, a Utah company,

Plaintiff,

v.

No. CIV 02-10 BB/LFG

3.47 ACRES OF LAND, COUNTY OF SAN JUAN, STATE OF NEW MEXICO, AUBREY D. and PATRICIA A. WOOD,

Defendants.

## MEMORANDUM OPINION EXCLUDING PIPELINE CORRIDOR THEORY

PRIOR to the trial, Plaintiff filed a motion pursuant to *Daubert v. Merrell Dow Pharmaceuticals, Inc.*, 509 U.S. 579 (1993), to prevent Defendants' experts from raising the "pipeline corridor" theory. "Expert evidence can be both powerful and quite misleading because of the difficulty in evaluating it." *Id.* at 595. The purpose of the *Daubert* analysis, therefore, "is to make certain that an expert, whether basing testimony upon professional studies or personal experience, employs in the courtroom the same level of intellectual rigor that characterizes the practice of an expert in the relevant field." *Kumho Tire Co. v. Carmichael*, 526 U.S. 137, 152 (1999). Thus, the litmus test is what experts actually do in the real world outside the courtroom. *Daubert v. Merrell*

*Dow Pharmaceuticals, Inc.*, 43 F.3d 1311, 1318 (9th Cir. 1995); *Karlin v. Foust*, 975 F. Supp. 1177, 1215 (W.D. Wis. 1997); *see also* 2 STEPHEN A. SALTZBURG, ET AL., FEDERAL RULES OF EVIDENCE MANUAL 1239 (7th ed. 1998) ("If the methodology is good enough for the real world, it is good enough for a trial. On the other hand, if the methodology is altered for purposes of litigation, there is every reason to exclude it after *Daubert*."). The Court concludes that no one in the real world uses the "pipeline corridor" theory to value ranch or residential land.

In an earlier ruling, the Court noted the possibility that a pipeline corridor could have additional value if someone not affiliated with the condemnor did the leg work of obtaining easements from multiple landowners and presented this as a ready-made corridor. It is also possible an easement could become so overburdened with pipelines or power lines it could have no other use and therefore result in an effective taking of the fee rather than the easement. Defendants presented no evidence of either situation. Rather, the Woods' land would continue to be used as agricultural land except that the condemnor should be charged by the rod and at a premium because other pipelines existed nearby. This demonstrates it was a preferable route to the processing plant and therefore the "theory" would result in a highest and best use as a pipeline corridor and a substantial multiplication of value. This is not a proper basis for valuation. *United States v. 77,819.10 Acres of Land*, 647 F.2d 104, 110 (10th Cir. 1981).

This application of the "theory" is completely theoretical and totally created for forensic purposes. Both of Defendants' expert appraisers originally evaluated the land at issue as ranch land (its present use) and residential property (a reasonably foreseeable future use). It was only after consultation with legal counsel and "further research" that they became aware of the pipeline corridor theory and neither expert had ever been involved with or even had knowledge of any real world sales in San Juan County where a willing buyer and a willing seller adopted this valuation method. Expert testimony deriving from techniques created for, and rooted exclusively in, the courtroom are suspect and must be examined very carefully under the judicial microscope. *Huey v. United Parcel Serv.*, 165 F.3d 1084, 1087 (7th Cir. 1999); *Moore v. Ashland Chem., Inc.*, 126 F.3d 679, 687 (5th Cir. 1997); *Black v. Rhone-Poulenc, Inc.*, 19 F. Supp. 2d 592, 603-4 (S.D.W. Va. 1998).

Application of the pipeline corridor theory to the facts of this case would also defy common sense. All Mr. Wood could offer as added value for the "pipeline corridor" across his property was that after condemnation he wanted to sell it as a pipeline corridor (but also continue to use it as pasture). It was his expressed intent to continue to graze cattle on this land just as he had done both before and after El Paso installed the original pipeline across this "corridor." Nonetheless, it is Defendants' theory that the corridor should become more valuable to each succeeding user. Not only is this application of the pipeline corridor theory contrary to logic, it also stands the whole concept of damages on its head. As the pipeline corridor becomes more established by each use, its value should increase so the land is actually enhanced, all the while the cattle continue to graze contentedly over the corridor. While at least one law student has advanced this theory,[1] it has been rejected by the courts addressing it directly.[2]

Application of the pipeline corridor theory here would also be contrary to both established New Mexico and federal law. *United States v. 77,819.10 Acres of Land*, 647 F.2d at 110; *United States v. 8.41 Acres of Land*, 680 F.2d 388 (5th Cir. 1982); *Yates Petroleum Corp. v. Kennedy*, 775 P.2d 1281 (N.M. 1989); *Board of Trustees of Town of Farmington v. B.J. Serv., Inc.*, 406 P.2d 171 (N.M. 1965).

Based on the above legal analysis and after hearing the experts' testimony, both before and during[3] trial, the Court concluded that whatever validity the pipeline corridor theory may have, it has no legitimate application to the facts of this case and would serve only to confuse the issues, mislead the jury, and waste time. Fed. R. Evid. 403. *United States v. Schmidt*, 711 F.2d 595, 598-99 (5th Cir. 1983). Therefore, in order

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1 Laura A. Haney, Comment: *Judicial Battles Between Pipeline Companies and Landowners: It's Not Necessarily Who Wins But By How Much*, 37 Hou. L. Rev. 125, 161-5 (2000). The unpublished Texas cases which Ms. Haney relied on have now been overruled by *Exxon Pipeline Co. v. Zwahr*, 88 S.W.3d 623 (Tex. 2002).

2 *Exxon Pipeline Co. v. Zwahr*, *supra*; *Exxon Pipeline Co. v. Hill*, 788 So. 2d 1154 (La. 2001).

3 All testimony was taken out of the presence of the jury.

to eliminate unjustifiable expense and delay, and to further the ascertainment of truth,[4] the Court precluded Defendants' experts from testifying on this theory. Fed. R. Evid. 102. *United States v. Call*, 129 F.3d 1402 (10th Cir. 1997) (jury might overvalue scientific sounding expert testimony which was not offered for legitimate purpose).

Dated at Albuquerque this 25[th] day of June, 2003.

BRUCE D. BLACK
United States District Judge

Counsel for Plaintiff:
Jon J. Indall, COMEAU MALDEGEN TEMPLEMAN & INDALL, Santa Fe, NM
James C. Brockmann, STEIN & BROCKMANN, Santa Fe, NM
Colleen Larkin Bell, QUESTAR REGULATED SERVICES COMPANY, Salt Lake City, UT

Counsel for Defendants:
J.E. Gallegos, Patricia Adele Matthews, Santa Fe, NM
Karen L. Townsend, Aztec, NM

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4 The Court did not preclude Defendants' experts from testifying on the highest and best use of the land for agricultural or residential purposes or on sales of comparable land for such purposes. Defendants, however, apparently chose not to call their experts Ms. Riley and Mr. Hunsperger to testify on these appraisals.

IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF NEW MEXICO

QUESTAR SOUTHERN TRAILS PIPELINE COMPANY, a Utah company,

Plaintiff,

v. No. CIV 02-10 BB/LFG

3.47 ACRES OF LAND, COUNTY OF SAN JUAN, STATE OF NEW MEXICO, AUBREY D. and PATRICIA A. WOOD,

Defendants.

MEMORANDUM OPINION AND ORDER
DENYING MOTION TO RECONSIDER *DAUBERT* RULING,
TO AMEND FINDINGS AND FOR NEW TRIAL

THIS MATTER is before the Court on *Defendants' Motion to Reconsider Daubert Ruling, to Amend Findings and for a New Trial* (doc. #235). The Court having duly considered the briefs of the parties, finds the motion must be Denied.

*Discussion*

*I.* *Reconsideration of Daubert Ruling*

A motion for reconsideration should not be used as a vehicle to relitigate matters already argued and disposed of. *Shields v. Shetler*, 120 F.R.D. 123 (D. Colo. 1988); *United States v. Western Elec. Co.*, 690 F. Supp. 22 (D.D.C. 1988). Rather, the relief sought by Defendants is extraordinary in nature and may be granted only in exceptional circumstances. *Servants of Paraclete v. Does*, 204 F.3d 1005 (10th Cir. 2000). No exceptional circumstances have been raised by Defendants.

Initially, it must be noted Defendants' motion is based on an incorrect factual premise, to-wit: "Our research has failed to find an appellate decision <u>upholding disqualification by a district court</u> of a qualified expert appraiser in an eminent domain case on the basis of the *Daubert* test or a *Daubert*-like exclusion." Defs.' Memo. Supp. at 2 (emphasis in original). This Court did not "disqualify" either of Defendants appraisers. Rather, the Court precluded them from testifying to a theory which lacked any foundation in present fact, law or logic. It is not applied by real experts to similar facts in the real world and would therefore likely confuse and mislead the jury. *See United States v. 8.41 Acres of Land*, 680 F.2d 388 (5th Cir. 1982). *See also United States v. Tran Trong Cuong*, 18 F.3d 1132, 1142 (4th Cir. 1994); Fed. R. Evid. 403.

Defendants representation regarding the lack of "an appellate decision upholding disqualification by a district court of a qualified appraiser" is also an inaccurate statement of the law. State appellate courts have upheld trial courts in condemnation cases when they refused to allow appraisers to testify to Defendants' pipeline easement theory over *Daubert* objections and indeed reversed the admission of such evidence. *See, e.g., Exxon Pipeline Co. v. Zwahr*, 88 S.W.3d 623 (Tex. 2002); *Westtex 66 Pipeline Co. v. Baltzell*, 2003 WL 21665312 (Tex. Civ. App. 2003); *Exxon Pipeline Co. v. Hill*, 788 So.

2d 1154 (La. 2001). Although Defendants now eschew the nomenclature "pipeline corridor," likely because of the *Hill* and *Zwahr* cases, the exact testimony tendered by Defendants herein was rejected in these decisions as well as *Westtex*.

In *Zwahr*, Exxon condemned a 50-foot easement to build a pipeline across the Zwahrs' 49-acre cotton farm. As in the present case, another pipeline already crossed the farm parallel to much of the proposed route. However, neither pipeline effected the Zwahrs' continued use of the surface for cotton farming. As in the present case, the Zwahrs' expert appraiser, Mr. Kangieser, valued the easement with "a value independent from that of the surface acreage, with a highest and best use as a pipeline easement." 88 S.W.3d at 626. Exxon's appraisers valued the land for farm and rural residential purposes at an amount approximately 5% of the value attested to by Kangieser using the pipeline easement theory. Holding the district court had erred in admitting the expert testimony based on pipeline easement value, the Texas Supreme Court recited Rule of Evidence 702 and quoted *Daubert v. Merrell Dow Pharmaceuticals, Inc.*, 509 U.S. 579 (1993). The Court concluded the testimony of Zwahrs' expert violated the before and after rule by valuing the easement separately for a pipeline:

> In reaching his highest-and-best-use conclusion, he relied, in part, on the existence of the Koch pipeline, which he believed created a probability that another pipeline would come in on or adjacent to that pipeline. He then researched the market for prices at which pipeline easements have sold, and based on those sales, estimated the value of the 1.01-acre tract as $36,077.

> Kangieser's testimony as a whole reveals that he premised his valuation on the fact of Exxon's condemnation, thus improperly including project enhancement in that valuation.

88 S.W.3d at 629.

As in the case at bar, the landowners also employed an expert to testify on the "per rod" value of a pipeline easement in *Exxon Pipeline Co. v. Hill.* In the consolidated appeal, one district court had admitted such testimony, one had excluded it under *Daubert.* Exxon's appraiser testified the highest and best uses were agricultural, residential or light industrial. Once again, based on other existing pipeline easements, plaintiffs' experts offered highly inflated values of the easements as a pipeline corridor. The Louisiana Supreme Court pointed out the fallacy of permitting appraisers to base their valuations strictly on pipeline easement values.

> The per rod comparables appear to show the value of the property as impacted by the expropriation itself, which is in stark contrast to existing expropriation law. Rods standing alone fail to consider many important attributes which insure proper valuation of land. As stated above, a landowner may be compensated $100 per rod for his property because his servitude was the last remaining parcel needed by a company. By contrast, the same landowner may only be paid $15 per rod because his is the first parcel purchased. Attempting to derive a system to value pipeline servitude by rods would lead to higher and unfair valuation of property.

788 S. 2d at 1164.

Although they initially appraised the land following the well recognized before-and-after technique, at trial Defendants' experts, Wayne Hunsperger and Laura Riley, advanced a per rod value more than twenty times higher than the value of Defendants' property as agreed upon by all of the appraisers using standard appraisal techniques. An appraisal advanced solely to artificially inflate the market value of property may properly be excluded. *See, e.g., Union Pacific R. Co. v. 174 Acres of Land*, 193 F.3d 944, 947-48 (8th Cir. 1999) (proper for trial court to exclude evidence of what a developer would pay for individual parcels of land if its highest and best use was residential, when land was being used as a farm at the time of the taking and no residential prospect).

Defendants also continue to argue New Mexico law supports the revised Hunsperger and Riley methodology. Contrary to Defendants' assertion, however, New Mexico law, like federal law, requires the determination of the "fair market value of the property, as a whole, before and after the taking." *Board of Trustees v. B.J. Serv., Inc.*, 406 P.2d 171, 173 (N.M. 1965); *Yates Petroleum Corp. v. Kennedy*, 775 P.2d 1281 (N.M. 1989); *United States v. 77,819.10 Acres of Land*, 647 F.2d 104 (10th Cir. 1981).

Finally, a motion for reconsideration must present matter that is likely to alter the outcome of the jury verdict. *Aldrich Enter., Inc. v. United States*, 938 F.2d 1134 (10th Cir. 1991). After counsel chose not to call Defendants' expert appraisers, Mr. Wood himself testified that based on the use of the land for prior easements it was worth $105,000. Rather than being persuaded by this pipeline easement testimony, the jury discounted Mr. Wood's testimony and awarded only $33,492.

II. *New Trial*

Federal Rule of Civil Procedure 59(a) provides for new trials when: 1) the fact finder's verdict is against the weight of the evidence; 2) the verdict is excessive or inadequate; 3) there is newly discovered evidence; 4) there is improper conduct by counsel or the court; or 5) there is improper conduct affecting the jury. *See Pool v. Leone*, 374 F.2d 961 (10th Cir. 1967); *Ahern v. Scholz*, 85 F.3d 774 (1st Cir. 1996). Defendants do not argue that any of these grounds apply. Rather, they base their argument on the Court's refusal to allow Mr. Hunsperger and Ms. Riley to testify on a per rod value of the land as a pipeline easement. Exclusion of expert testimony which would not have assisted the jury in their search for truth does not warrant a new trial. *Holt v. Utility Trailers Mfg. Co.*, 494 F. Supp. 510 (E.D. Tenn. 1980).

III. *Conclusion*

Defendants have failed to show that there are any exceptional circumstances that would require reconsideration of the Court's *Daubert* ruling precluding valuation solely on a pipeline corridor methodology for appraising easements on the present facts. The Court's findings are not "clearly erroneous," but, rather, supported by the record. Indeed, this is precisely the type of circumstances in which *Daubert* should shut the gate on novel, unorthodox theories which are created solely for purposes of litigation. Defendants are thus, yet again, simply attempting to relitigate matters that have already been decided.

Now, therefore,

IT IS ORDERED that *Defendants' Motion to Reconsider Daubert Ruling, to Amend Findings and for a New Trial* is DENIED.

DATED at Albuquerque this 31st day of July, 2003.

BRUCE D. BLACK
United States District Judge

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FAIR White Paper on Valuation: Exhibit H

United States District Judge B. Lynn Winmill's Opinion and Order, Northwest *Pipeline Corp. v. 95.02 Acres of Land*, U.S.D.C. Cause No. CV-01-628-E-BLW (D. Idaho, December 19, 2003)

IN THE UNITED STATES DISTRICT COURT

FOR THE DISTRICT OF IDAHO



NORTHWEST PIPELINE CORPORATION,

Plaintiff,

v.

95.02 ACRES OF LAND, more or less, in Power County, Idaho; UNITED STATES OF AMERICA; LEE BEAR, et al.; and UNKNOWN OWNERS,

Defendants.

Case No. CV-01-628-E-BLW

**MEMORANDUM DECISION AND ORDER**

## INTRODUCTION

Pending before the Court is Plaintiff Northwest Pipeline's (Northwest's) Motion *In Limine* to Preclude Trial Testimony by Defense Experts. Northwest seeks to exclude the proposed testimony of Thomas Tulk, Ed Morse, and Robert E. Grijalva – expert witnesses for the Defendants. Northwest asserts that the proposed testimony of these expert witnesses on the issue of just compensation is in direct and irreconcilable conflict with the proper measure of just compensation allowed by federal law and that their testimony should therefore be excluded. The

Court, based upon its review of the parties' briefing and oral argument, and for the reasons set forth below, largely agrees with Northwest's position.

## BACKGROUND

Since 1955, Northwest Pipeline Corporation ("Northwest") has operated a multi-state natural gas pipeline that crosses part of the Fort Hall Indian Reservation ("Reservation"). Up until 1995, Northwest had a contractual right to operate its pipeline across the Reservation. In 1992, Northwest sought consent to construct a second pipeline along the existing easement and to extend its contractual right to cross the Reservation. Shortly thereafter, Northwest began construction on the second pipeline believing that it had been granted consent to do so. However, following a series of communications between the Bureau of Indian Affairs ("BIA"), Northwest, and representatives from the Reservation, the BIA issued a letter to Northwest in May of 2000 declaring that Northwest was trespassing on the Reservation. Northwest unsuccessfully challenged the BIA's finding through an administrative procedure. Northwest then appealed the administrative decision to this Court. The suit, *Northwest Pipeline Corporation v. Gale A. Norton, et al.,* Case No. CIV 01-192-E-BLW, was dismissed on the grounds that Northwest did not timely file for appeal.

In December 2001, Northwest filed this action before the Court seeking condemnation of an easement across allotment lands on the Fort Hall Indian Reservation under 25 U.S.C. § 357. Central to this action is the amount Northwest must compensate the reservation landowners for condemning an easement across their property. Several experts have been retained in order to aid this process, including Defendants' experts: Thomas Tulk, Ed Morse, and Robert E. Grijalva.

## DISCUSSION

Any time expert evidence is offered at trial, a trial judge is charged with a duty to determine whether the evidence is both reliable and relevant. *See* Federal Rule of Evidence 702; *Daubert v. Merrell Dow Pharmaceuticals, Inc.*, 509 U.S. 579, 597 (1993). Rule 702 of the Federal Rules of Evidence "requires that the [expert] evidence or testimony 'assist the trier of fact to understand the evidence or to determine a fact in issue.' This condition goes primarily to relevance." *Id.* at 591. Rule 702 "clearly contemplates some degree of regulation of the subjects and *theories* about which an expert may testify." *Id.* at 589 (emphasis added). Therefore, "the trial judge must determine at the outset, pursuant to Rule 104(a) whether the expert is proposing to testify to (1) scientific, [technical, or other specialized knowledge] that (2) will assist the trier of fact to understand or determine a fact in issue." *Id.* at 592. If an expert's theory is at odds with the governing legal standard, it is therefore not relevant to the matter at hand and must be excluded by the court. *See e.g., See United States v. 8.41 Acres of Land*, 680 F.2d 395, (5th Cir. 1982).

**Standard of Law Concerning Valuation in a Condemnation Action**

When private land is condemned to serve a public purpose the condemnor must provide the property-owner with just compensation. *See* U.S. Const. amend. V; Idaho Const. Art. I § 14.[1] "Just compensation has often been said to be the fair market value of the property taken, or what a willing seller could receive from a willing purchaser." *See United States v. Weyerhaeuser Comp.*, 538 F.2d 1363, 1366 (9th Cir. 1976); 4 *Nichols on Eminent Domain* § 12.02 (3d ed. 2003).[2] "Fair market value takes into consideration:

> (t)he **highest and most profitable use** for which the property is adaptable and needed or likely to be needed in the reasonably near future . . . to the full extent that the prospect of demand for such use affects the market value

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[1] In most condemnation actions, the land is condemned by the government. Private parties however, may also condemn land if such power is delegated to them pursuant to statute. *See e.g.*, 25 U.S.C. § 357; I.C. §§ 7-701 through 7-721 . In addition, the Court notes that any rules applicable to the Government as condemnor are also applicable to private parties. *See generally* 1A *Nichols on Eminent Domain* § 3.03 (3d ed. 2003); 26 Am. Jur. 2d *Eminent Domain* § 327 (1996).

[2] The appropriate measure of damages in a partial-taking case, as is the case here, is the difference between the value of the parent tract before the taking and its value after the taking. "When the property interest taken from a parent tract is merely an easement, the proper measure of damages is still the before-and-after method of valuation, expressed as the difference between the market value of the land free of the easement and the market value as burdened with the easement." *See United States v. 8.41 Acres of Land*, 680 F.2d 388, 392 (5th Cir. 1982).

while the property is privately held."

*See Weyerhaeuser* 538 F.2d at 1366 (quoting *Olson v. United States*, 292 U.S. 246, 255 (1934) (emphasis added).

One of the most generally-accepted methods to determine fair market value is the sales comparison method. *See United States v. 22.80 Acres of Land*, 839 F.2d 1362, 1364 (9th Cir. 1988). An appraiser using the sales comparison method analyzes recent sales of comparable land located within the vicinity to determine the value of the land at issue. If such sales exist, the sales prices of those other properties are adjusted to compensate for the differences existing between them and the subject property.[3]

"The fair market value standard does not, however, compel consideration of all possible factors which might enhance the value of the property condemned." *Weyerhaeuser* 538 F.2d at 1366. For instance, any enhanced value due to the condemnor's need for the land is disregarded. *See United States v. Cors*, 337 U.S. 325, 332 (1949) ("It is not fair that the government be required to pay the enhanced price which its demand alone has created . . . It does not reflect what a willing buyer would pay in cash to a willing seller"); *Weyerhaeuser Co.*, 538 F.2d

[3] Only two of Defendants' experts, Morse and Grijalva, utilized the sales comparison method.

at 1366 ("values resulting from the urgency or uniqueness of the government's need for the property . . . do not reflect what a willing buyer would pay to a willing seller"). In other words, value peculiar to the condemnor is not relevant to the just compensation calculation. *Weyerhaeuser* 538 F.2d at 1366; *United States v. Cors*, 337 U.S. 325, 332 (1949) ("The special value to the condemnor as distinguished from others who may or may not possess the power to condemn has long been excluded as an element from market value"); 4 *Nichols on Eminent Domain* § 12.03 (3d ed. 2003) ("just compensation in the constitutional sense is what the owner lost, not what the condemnor has gained"). The policy against enhancing value based upon the condemnor's need is often referred to as the "project enhancement rule."[4] There is however, an exception to the project enhancement rule. If the land is especially adapted for the proposed purpose and consequently creates a "*special demand* by ordinary purchasers in the ordinary market," then the owner is entitled to claim additional value based upon the proposed purpose." *See* 4 *Nichols on Eminent Domain* § 12.03 (3d ed. 2003) (emphasis added). Therefore, before a court will consider added value based upon the proposed project of the

[4] Defendants, relying upon dicta in *Desert Citizens Against Pollution v. Bisson*, 231 F.3d 1172 (9th Cir. 2000), argue that the project enhancement rule applies only to the Government as condemnor and not to private party condemnors. The Court finds that this argument is without merit. *See supra* note 1.

condemnor, the defendants must demonstrate that there are others interested in buying the land and using it for the same purpose. *See United States v. Whitehurst*, 337 F.2d 765, 772 (4th Cir 1964) ("Mere physical adaptability to a use does not establish a market. In ascertaining the demand, the requirements of the [condemnor] for the project for which the land is taken must be totally excluded") *cited with approval in Weyerhaeuser* 538 F.2d at 1367. The Court notes that this exception is very narrow given that "[t]he very purpose of reserving in the people the power of eminent domain is to prevent an owner of a site especially available for a public work, but not of great value for other purposes, from trading upon the necessities of the public . . . and from compelling the public to pay for his land whatever figure he may name . . . ." 4 *Nichols on Eminent Domain* § 12B.16 (3d ed. 2003); *see also McGovern v. New York*, 229 U.S. 363, 371-72 (1913) ("[An] owner is not permitted to take advantage of the necessities of the condemning party").

**Thomas Tulk**

First, the Court will address Northwest's objections to defense expert Thomas Tulk. Northwest argues that Tulk's computation of just compensation is irrelevant to the current action because it is based upon the "Opportunity Cost Doctrine." According to Tulk's appraisal report "[t]he Opportunity Cost Doctrine suggests that the upper bounds for the payment of the right to pass through American Indian lands is the alternative cost that would confront [Northwest] were they required to re-route their project so that it did not pass through the reservation." *See* Affidavit of Jason Scott (Docket No. 138) Exhibit A at 11 (emphasis in original). Although Tulk's report provides some evidence that the Opportunity Cost Doctrine has been utilized in contract negotiations for easements across Indian reservations, *see id.* at Exhibit A at 22-23,[5] the Court finds that it is not an appropriate measure of just compensation in a condemnation action. Tulk's damage calculation does not measure the property owners' loss, but rather impermissibly calculates the value of the land to Northwest and trades upon the urgency of Northwest's need. *See United States ex rel. TVA v. Powelson*, 319 U.S. 266, 281 (1943) ("It is a well settled rule that . . . it is the owner's loss, not the taker's gain, which is the measure of compensation for the property taken"); 4 *Nichols on Eminent Domain* § 12.03 (3d ed. 2003) ("just compensation in the constitutional sense is what the owner lost, not what the condemnor has gained"). Therefore, the Court finds that any calculation of damages under the Opportunity Cost Doctrine directly and irreconcilably conflicts with the project enhancement

[5] In addition, defense counsel stated that she could provide case citations for cases where administrative courts have applied the Opportunity Cost Doctrine. Counsel has failed to do so and the Court is unaware of any courts that have adopted the Opportunity Cost Doctrine.

rule – that is, that any value peculiar to a condemnor is not relevant to the just compensation calculation. *See Weyerhaeuser* 538 F.2d at 1366. The Court will therefore exclude Tulk's proposed expert testimony on the basis of Federal Rules of Evidence 702 and 402.

Tulk's report also includes an opinion that Northwest is liable for trespass penalties and opines that these penalties "could amount to tens-of-millions of dollars." *See* Affidavit of Jason Scott (Docket No. 138) Exhibit A at 14. Previously, the Court ruled that Defendants may not, in this action, seek damages relating to any injury resulting from Northwest's trespass.[6] *See* Memorandum Decision and Order at 10-11 (Docket No. 75). Therefore the Court will not allow Tulk to testify as to any damages relating to the trespass.[7]

**Ed Morse**

Northwest also has several objections to expert Ed Morse's proposed testimony. Northwest's first objection rests upon the fact that Morse's report includes an amount of just compensation that correlates not only to the value of

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[6] The Court notes however, that Defendants are free to maintain a separate action to recover any damages resulting from the trespass.

[7] Northwest also claims that Tulk is not qualified to testify regarding property appraisals and that his proposed testimony must be excluded because it does not separately value each individual allotment. However, in light of the Court's finding that all of Tulk's proposed testimony is irrelevant, the Court need not reach these issues..

the real property, but also to the improvements thereon that were created by Northwest.[8] Northwest argues that it was improper for Morse to include an amount attributable to the pipeline itself and to rely upon the common law rule that "a trespasser who builds on another's land dedicates his structure to the land's owner."

The Court acknowledges the common law rule; however, the Ninth Circuit has noted approvingly that "some courts have recognized an exception to the forfeiture rule where a body has the power to exercise eminent domain. '[T]he general rule as to things affixed to the freehold by a trespasser . . . is not applicable as against a body having the power of eminent domain, and entering without leave, and making improvements for the public for which it was created and given such power.'" *See Etalook v. Exxon Pipeline Company*, 831 F.2d 1440, 1444 (9th Cir. 1987) (quoting *Anderson-Tully Co. v. United States*, 189 F.2d 192, 197 (5th Cir. 1951)). Similarly, the Court finds that an owner whose property is condemned is not entitled to compensation for improvements erected thereon by the condemnor at a time when the condemnor occupied the premises as a lessee, as is the case here. *See Anderson-Tully Co. v. United States*, 189 F.2d 192, 197 (5th

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[8] Northwest also alleges that Morse failed to adequately appraise each individual allotment and that therefore his testimony must be excluded. The Court finds however, that Morse did conduct a separate appraisal for each allotment. *See* Affidavit of Jason Scott (Docket No. 138) Exhibit B at 29-30.

Cir. 1951); *Cf. Alaska v. Teller Native Corp.*, 904 P.2d 847, 851-52 (Alaska 1995) (holding that condemnor must compensate landowner for value attributable to improvements made by condemnor during leasehold). Moreover, the Court finds that, if it were to require Northwest to compensate the landowners for the increased value due to the pipelines, the property owners would be unjustly enriched. *See Etalook v. Exxon Pipeline Company*, 831 F.2d 1440, 1445 (9th Cir. 1987). Therefore, the Court finds that Morse may not testify that the existing pipelines increase the value of the land for purposes of determining just compensation.[9]

Northwest next argues that Morse may not be allowed to testify at trial concerning any damages relating to survey costs. In his report Morse states that, because Northwest failed to "survey and record the easement boundaries," eventually the landowners will be forced to do it on their own. *See* Affidavit of Jason Scott (Docket No. 138) Exhibit B at 33. Morse opines that the survey costs will amount to approximately $39,000. *See id.* Defendants failed to respond to this objection. Therefore, pursuant to Local Rule 7.1(f), the Court will deem Northwest's motion unopposed and prohibit Morse from testifying about possible damages relating to survey costs.

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[9] Defendants argue that the holding in *Etalook* does not apply to private parties with the power of eminent domain. The Court finds this argument lacks merit. *See supra* note 1.

**Best Use- Ed Morse and Robert Grijalva**

Northwest also states that it was error for both Morse and Grijalva to calculate the value of the land as anything other than farmland or grazing land. In their reports, both Morse and Grijalva state that the land in question should be valued based upon its best use and opine that its best use is as a natural gas corridor, given that the pipelines are already in place. Both appraisers then utilize the comparative sales approach to determine the value of the land. *See* Affidavit of Jason Scott (Docket No. 138) Exhibit B at 26-28 & Exhibit C at 29-30 (listing comparative sales of pipeline corridors).

The Court finds, however, that the project enhancement rule renders both Morse's and Grijalva's calculations irrelevant absent evidence that purchasers other than Northwest are interested in buying the land, or land in the vicinity, for use as a pipeline corridor. *See United States v. Cors*, 337 U.S. 325, 332 (1949) ("The special value to the condemnor *as distinguished from others who may or may not possess the power to condemn* has long been excluded as an element from market value") (emphasis added); 4 *Nichols on Eminent Domain* § 12.03 (3d ed. 2003). Defendants have failed to present any convincing evidence that other parties are, or would be, interested in buying the land, or land in the vicinity, for use as a pipeline corridor.[10] Given the lack of proof concerning a market for pipeline corridors in the relevant vicinity, the Court finds, pursuant to the project enhancement rule and Rule 402of the Federal Rules of evidence, that experts Morse and Grijalva may not testify that the value of the land should be calculated as a pipeline corridor.

## ORDER

NOW THEREFORE IT IS HEREBY ORDERED that Plaintiff's Motion In Limine to Preclude Trial Testimony By Defense Experts (Docket No. 136) is GRANTED.

Dated this 19th day of December, 2003.

B. LYNN WINMILL
Chief Judge, United States District Court

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[10] The United States pointed out that there is a Chevron petroleum pipeline that also runs through the Reservation. However, the Court does not find this evidence sufficient to show a market for utility corridors across the Reservation. In addition, the Government has admitted that "the Bureau of Indian Affairs has never received any request by any utility entity other than Northwest for an easement upon any portion of the land described" in Northwest's complaint. *See* Supplemental Affidavit of Jason D. Scott Exhibit A at 13 (Docket No. 161).

Defendants also submitted a supplementary affidavit after oral argument that relates to Northwest's acquisition of an easement across the Umatilla Indian Reservation, located in Oregon. The court finds that this affidavit is irrelevant because it is not evidence that there is a market for the land at issue in this case.